

The London School of Economics and Political Science

Investor protection and equity markets: an Evaluation of private enforcement of related party transactions rules in Russia

Vladimir Meerovitch

A thesis submitted to the Department of Law of the London School of Economics for the degree of Doctor of Philosophy, London, March 2014

Declaration

I certify that the thesis I have presented for examination for the PhD degree of the London School of Economics and Political Science is solely my own work other than where I have clearly indicated that it is the work of others (in which case the extent of any work carried out jointly by me and any other person is clearly identified in it).

The copyright of this thesis rests with the author. Quotation from it is permitted, provided that full acknowledgement is made. This thesis may not be reproduced without my prior written consent.

I warrant that this authorisation does not, to the best of my belief, infringe the rights of any third party.

I declare that my thesis consists of 96,351 words.

Acknowledgements

Researching and writing this thesis introduced me to many inspiring people. One way or another, they all made a mark on the final product. I apologise for not listing them all here.

In the first place, my thanks go to Dr Eva Micheler, who got me started on the project and patiently supervised its progress over the course of some seven years. Thanks to Eva's editorial advice, rough notes and ideas turned into draft chapters. Professor Paul Davies provided valuable insights during the formative stages. Dr Carsten Gerner-Beuerle tirelessly reviewed and re-reviewed the three substantive chapters that make up the core analytical and evidential part of the thesis. Carsten and Professor David Kershaw helped me see the project through to the end and I am particularly grateful for their assistance during the hectic final months leading up to submission. Throughout, the supportive research environment in the Law Department at the LSE kept me going. Thanks are therefore due to Professors Colin Scott, Andrew Murray, and Linda Mulcahy, the Department's research directors and the Department's research students (too numerous to list; but they know who they are) who were instrumental in fostering that environment while I pursued my research.

At various points alongside the thesis, I had the pleasure of working with Professors Cees van Dam, Doreen McBarnet and Monty Raphael QC. Not only did I pick up invaluable research skills from these very erudite individuals but also earned much needed money to be able to continue with the research project. My employer Peters & Peters Solicitors has exhibited the understanding and flexibility to accommodate the sporadic work patterns of my academic pursuit rarely seen in the City.

I am fortunate to have a very loving family. My mum and dad Raisa and Iosif, my brother Vladislav, my in-laws Marion, Stan (who sadly passed away shortly before submission), Caroline and Nathan were always there to offer an often needed escape and shoulders to lean on. Without the endless patience, selflessness and support of my wife Louisa, this thesis would not have been possible. Without my dad's faith and optimism this thesis would never have been finished. It is to him that I dedicate this thesis.

Abstract

The aim of my thesis is to investigate the relationship between legal protections of minority shareholders – ‘on the books’ and ‘in action’ – and the development of equity markets. In this regard, there is a general consensus that Russian legal measures adopted to protect minority shareholders are strong. The failure of the judiciary to enforce these measures is the principal focus of the academic criticism and has been frequently cited to explain the underdevelopment of the Russian equity market. Notably, the criticism of the judiciary persists despite the market’s marked improvements over the last decade. And yet there has been little empirical analysis of enforcement of the minority shareholder protections by Russian judiciary. This thesis examines private enforcement of corporate law in Russia focusing on the lawsuits to impugn transactions with corporate insiders and the outcomes of those suits. Drawing on a dataset of 170 cases decided by the Federal Arbitrazh Court for the Moscow region in 1999 – 2006, the thesis finds that a large proportion of claimants are unsuccessful. Relying primarily on the law and economics literature and theoretical accounts of the relationship between the law and market development, the thesis develops an analytical framework (for convenience termed judicial bias hypothesis) against which it evaluates case outcomes. The evaluation suggests that in a substantial fraction of the cases the outcomes were justified by legislation or by efficiency, casting doubt over the criticisms of Russian judiciary. While cautious in drawing causal links between the enforcement and markets, the thesis suggests that marginalising legal institutions’ role in Russia might be premature. Their role in fostering the market might be greater than anticipated particularly in incentivising disclosure if not in deterring overreaching.

CONTENTS:

CHAPTER 1 INTRODUCTION

<i>Introduction</i>	1
1.1 Why Enforcement? Why Russia?	2
1.2 Case Data and Research Methods.....	7
<i>Plan of the thesis</i>	16

CHAPTER 2 A JUDICIAL BIAS HYPOTHESIS

<i>Introduction</i>	17
2.1 The Problem	18
2.2 Investor Protection	22
2.3 Welfare Maximisation	23
2.3.1 Goshen's efficiency framework	26
2.3.2 Hypothetical bargaining model	30
2.3.3 Transaction Costs	32
2.3.4 Verifiability	33
2.3.5 Information Asymmetries	35
<i>Deterrence</i>	36
<i>Information Revelation</i>	40
<i>Hypothesis</i>	59

CHAPTER 3 PROCEDURAL RULES IN COMPANY ACTIONS

<i>Introduction</i>	60
3.1 Problems with company enforcement of Part XI JSCA.....	61
3.1.1 Suboptimal enforcement problems	61
3.1.2 Improper enforcement problems	65
3.2 Law	70
3.2.1 Transaction characterisation	72
3.2.2 Knowledge attribution under article 181(2)	77

3.3 Analysis	81
3.3.1 Transaction characterisation	82
3.3.2 Knowledge attribution under article 181(2)	85
<i>Solvent claims: the contract-based standard</i>	87
<i>Insolvent claims: the appointment-based standard</i>	92
<i>Insolvent claims: the contract-based standard</i>	96
3.4 Hypothesis	105
3.5 Case data	105
3.5.1 Insolvent cases	108
3.5.2 Solvent cases	122
<i>Conclusion</i>	131

CHAPTER 4 SHAREHOLDER *LOCUS STANDI*

<i>Introduction</i>	134
4.1 Problems with minority shareholder enforcement of Part XI JSCA.....	136
4.1.1 Suboptimal enforcement problems	136
4.1.2 Improper enforcement problems	141
4.2 Shareholder <i>locus standi</i> under Part XI JSCA.....	143
4.2.1 Law	143
4.2.2 Judicial treatment of shareholders' <i>locus standi</i> under Part XI JSCA	149
<i>Literature on the locus standi prior to the August 2001 reform</i>	149
<i>Literature on the rights and interests requirement</i>	151
4.2.3 Case data	157
<i>Conclusion</i>	165

CHAPTER 5 PROCEDURAL RULES IN SHAREHOLDER ACTIONS

<i>Introduction</i>	168
5.1 Statue of limitations	169
5.1.1 Introduction	169

5.1.2 Analysis	171
<i>Insider claims: the contract-based standard</i>	171
<i>Outsider claims: disclosure-based standard</i>	178
<i>Avoidance of statute of limitations</i>	186
5.1.3 Hypothesis	188
5.1.4 Case Data	189
<i>Insider cases</i>	192
<i>Outsider cases</i>	196
5.2 Contemporaneous ownership rule	202
5.2.1 Analysis	203
5.2.2 Hypothesis	210
5.2.3 Case data	211
<i>Conclusion</i>	216
CHAPTER 6 CONCLUSION	
<i>Introduction</i>	217
6.1 Irrelevance	217
6.2 Detriment	224
6.3 Facilitation	227
APPENDIX 1 CONSULTANT+ AND OTHER STATISTICAL DATA	2a
APPENDIX 2 CASE DATA	15a
APPENDIX 3 OTHER JUDICIAL DECISIONS CITED IN THE THESIS.....	38a
BIBLIOGRAPHY	41a

CHAPTER 1

INTRODUCTION

Introduction

Correlation between stock market development and long-run economic growth has acceptance in academic literature and policy statements issued by the development institutions.¹ Risk diversification, liquidity, information processing, capital mobilisation, firm discipline and facilitation of alternative remuneration mechanisms are just some of the services stock markets offer to facilitate economic growth, particularly important for the developing and transition countries (Levine, 1997; Black, 2001: 835-838). Building stock markets, however, is less than straightforward – indeed ‘magical’ (Black, 2001: 782). To what extent the law, ‘on the books’ and ‘in action’, can contribute to the development of the stock markets and hence economic growth is an important issue not only for the policy makers concerned with economic development but also for the legitimacy of the mandatory corporate law. Unsurprisingly then, the issue, as this Chapter endeavours to show, is hotly contested.

The Chapter introduces the thesis and, as an introduction, its goals are twofold. First, it explains why an empirical study of private enforcement of anti-self-dealing rules in Russia is worthwhile pursuing (section 1.1). Second, it deals with research methods including how the empirical data was obtained and explains which aspects of the data will be taken up in subsequent Chapters, and why (section 1.2). The plan of the thesis is outlined at the end of the Chapter.

¹ See presentation by Gerard Caprio (Director, Financial Sector Policy and Strategy Department, in the World Bank’s Financial Sector Vice Presidency) emphasizing ‘a clear causal link between finance and development’, presented at the World Bank’s Financial Sector Policy Global Dialogue Series, Session 8: Finance for growth: policy choices in volatile world. Available at http://www1.worldbank.org/finance/assets/images/financeforgrowth_english.pdf. Accessed on 1 November 2013.

1.1 Why Enforcement? Why Russia?

In the late 1990s a group of scholars studied and established a correlation between legal rights attributed to outside investors and the extent of stock market development in forty-nine countries around the world (La Porta et al, 1998, 1999, 2000). Other studies appeared to support what has now become known as the ‘law matters thesis’, for example, by illustrating that voting class of shares is valued significantly more in countries with weaker investor protections (Nenova, 2003), and that companies incorporated in jurisdictions with weak corporate laws are more likely to cross-list their securities in other jurisdictions than firms incorporated in jurisdictions with strong corporate laws (Reese and Weisbach, 2002). In the similar vein, Johnson et al demonstrate correlation between the extent of investor protection and the depth of financial market crises (2000). Pistor et al find support, in the context of transition economies adding, however, that the quality of enforcement may have an even stronger explanatory force than the ‘law on the books’ (2000). Bebchuck extended the law matters thesis to the separation of ownership and control *a la* Berle and Means by demonstrating that such a separation could not occur in the presence of high private benefits of control (1999).² It appeared therefore that ‘[i]t may be better to have contracts restricted by laws and regulations that are enforced than unrestricted contracts that are not’ (La Porta et al, 2000: 7). While La Porta et al did not invent the ‘law matters’ thesis,³ their work marked a turning point in a number of directions in academic and policy debates, the most controversial of which were ‘implicit claims of superiority for outsider shareholder-oriented norms’ (Dignam and Galanis, 2009: 47).

Prior to La Porta’s et al work the understanding of the relationship between law and equity markets was dominated by the neoclassical law and economics literature, which opposes state intervention to reduce private benefits of control and other agency costs of outside equity.⁴ Firstly, it is argued that agency costs are not synonymous with market failure and can be sufficiently overcome by private ordering; secondly, transaction cost obstacles to private

² Under such conditions control would only be sold as a ‘package’ because dispersed owners would not be able to take advantage of private benefits and hence would not pay control premium.

³ The idea can be traced back to the modernisation movement that followed Weber (Ginsburg, 2000)

⁴ Private benefits of control are the ‘residual loss’ component of the agency costs of outside equity, the other two components being the costs of monitoring and bonding efforts exerted by minority shareholders and corporate insiders respectively. Private benefits of control represent some value not shared among all the shareholders in proportion to the shares owned but that is enjoyed exclusively by the party in control (Dyck and Zingales, 2004; Jensen and Meckling, 1976).

solutions can be addressed by the provision of default terms which parties may modify to suit their circumstances; and thirdly, state regulation via mandatory law is unlikely to yield results superior to those prevalent in an imperfect market. The costs of mandatory law could outweigh its benefits thus generating inefficient allocation of resources.

The first argument asserts that existence of agency costs does not necessarily lead to misallocation of the society's resources. Misallocations occur in cases where firms are able to externalise their production costs and thus charge lower prices for their outputs. Since lower prices lead to higher demand, such firms will respond by increasing their output with the ultimate outcome being over-production from the society's point of view (Cheffins, 1997: 521-524). The agency costs of outside equity, on the other hand, are substantially internalised by the corporation. Jensen and Meckling formally illustrate that agency costs are borne by issuers so long as the equity market anticipates them (1976). Prospective minority shareholders realise that the insiders' interests will diverge somewhat from theirs and reflect the effect of the divergence in the price they pay for shares (Jensen and Meckling, 1976: 313). In effect insiders pay the price for the ability to extract private benefits of control.

The impact of market forces, in turn, ensures reduction of control rents and other agency costs. Competition in product, labour and capital markets on the one hand and entrepreneur's self-interest in maximising his/her returns on the other, produce pressure to reduce firm's cost of capital. Given the correlation between cost of capital and agency costs, the pressure to reduce the former acts as an incentive to minimise the latter. In other words, insiders have the incentives to impose constraints on their ability to extract control rents. Moreover, the benefits of these constraints outweigh the costs since neither the insider nor outside shareholders are likely to accept arrangement where their position is made worse off. The possibility of repeat transactions and inclusion of constraints as enforceable terms into corporate charter assures credibility of the reached arrangement (Easterbrook and Fischel, 1991: 95, 8-22). Furthermore, provided costs of reaching the agreement are sufficiently low, the parties will achieve the optimal arrangement regardless of legal provisions on the matter. According to the Coase theorem, law does not matter when transaction costs are zero (Coase, 1988: 14):

'... in the absence of transaction costs, it does not matter what the law is, since people can always negotiate without cost to acquire, subdivide, and combine rights whenever this would increase the value of production.'

The second and third arguments provide responses to the introduction of transaction costs into above analysis. These include search and information costs, bargaining and decision costs, policing and enforcement costs (Dahlman, 1979). Transaction costs could prevent private parties from solving their problems in a socially optimal manner and could therefore sanction state intervention. The essence of the second argument is insignificance of the transaction costs in the context of the insiders – outside shareholders relationship in firms listed on stock exchanges. The argument rests on the efficient market hypothesis according to which stock prices accurately reflect all public information in relation to a security (Gilson and Kraakman, 1984). Once this hypothesis is acknowledged, it no longer matters that negotiation costs prevent arrangement suitable to *all* outside shareholders from being reached. As Easterbrook and Fischel amply explain, even if entrepreneurs pick terms out of a hat, '[t]hey cannot force investors to pay more than the resulting investment instrument is worse' (1991: 17). In fact, those investors who disapprove of the arrangement do not have to buy the security at all.

Furthermore, the hypothesis implies that incapacity of some investors to price the arrangement correctly due to the costs of obtaining and digesting all the information is immaterial. This is because the price of stock is established by professional investors who learn the details of security to beat the market. The process of trading between these informed traders impounds the information into the price of the security. In other words casual investors are price protected, whereas enabling corporate law consisting of default terms that parties could alter to reflect the circumstances particular to their situation could address the transaction costs (Easterbrook and Fischel, 1991:18).

Finally, state intervention on the basis of mandatory law is criticised. Essentially critique asserts that regulation of corporate affairs via mandatory law would bring about suboptimal outcomes to those prevalent in imperfect market. The reasons are that firms vary in their characteristics and operate in a constantly changing economic environment, which imply the absence of an 'one size fits all' solution to the needs of participants in corporate affairs. The danger is that mandatory rules may preclude the parties from reaching mutually beneficial arrangements that suits their circumstances. Moreover, legislators are unlikely to have the same level of expertise and information as the market participants to be able to produce adequate sets of rules. Periodic and protracted nature of the law reform process exacerbates this problem. Overall this means that many firms will be stuck with inefficient terms, that do not reflect their needs, for the most of the time. It is true that often firms are able to

overcome adverse effects of mandatory rules by restructuring their contractual transactions but this process carries costs for the firms and thus for the society (Cheffins, 1997: 227-236; Macey, 1993: 193-211; Black, 1990: 551-561; Siems, 2008: 233).

In sum, to the extent mandatory provisions do not prevent insiders and investors from establishing governance arrangements that suit their circumstances corporate law can be described as trivial. To the extent that such provisions impose unnecessary transaction costs on market actors corporate law should be trivial in the sense that it should operate on the basis of default provisions (Black, 1990: 544; Romano, 1989).

It is perhaps unsurprising then that attempts have been made to reconcile La Porta's findings with the triviality thesis. Thus, Coffee has persuasively argued that it is only once outside shareholders become a powerful lobby group, do strong investor protection measures follow (Coffee, 2001). Other commentators have suggested that variables other than law provide better explanation for the dispersion of shareholding and, implicitly, stock market development. Thus, Roe's politics thesis contends that in countries with strong social democracy entrepreneurs need to retain control of the corporation in order to maintain a counterbalance to other claimants on the firm, namely labour and government. This precludes them from selling shares and thus diffusion does not occur and markets do not develop (Roe, 2003; Fox and Heller, 2000). Licht provides thesis rooted in nations' cultures (2001). He maintains that, to the extent that national culture precedes law, culture is the ultimate variable that determines regulation and development of stock markets.⁵ There are important methodological problems with the law matters thesis also (Siems, 2008: 9).

But the fact that in the countries with vibrant markets law played little role in assisting their development also contradicts law matters thesis is particularly relevant to the present analysis. Experiences in the USA and the UK, arguably countries with the most developed markets in the world, show that laws were not enforced in the former and took 'laissez-faire' approach to minority protection in the latter at times when both countries experienced rampant growth of their markets (Coffee, 2002: 93-100; Cheffins, 2001: 468-482). This has lead a number of scholars to examine whether the strong rules identified in these jurisdictions are actually enforced in practice (Armour et al, 2009 and work cited therein). In other words,

⁵ Licht's argument is comparable to an earlier critique of the modernisation movement in law and development studies made by Trubeck and Galanter (1974).

empirical evidence on private enforcement offers valuable contribution to what is still an unsettled debate.

And it is here that Russia as a jurisdiction becomes particularly interesting to study. The core legislation for the protection of outside shareholders from insider overreaching is the Russian Joint Stock Companies Act of 1996 (JSCA),⁶ which is based on the self-enforcing model of corporate law devised by a team of academics lead by Professors Black and Kraakman (Black and Kraakman, 1996; Black, Kraakman and Tarassova, 1998) (JSCA drafters). This model resonates law matters thesis in at least two ways. First, it provides strong protections for outside shareholders by means of mandatory law. Secondly, the model relies on structural (procedural) constraints based on simple, bright-line rules backed by strong remedies. In this way importance of enforcement is emphasised and placed directly in the hands of the participants thus reducing the reliance on the judiciary to the possible minimum (1996: 1933-1937).

Despite the ingenuity of self-enforcing Russian law its promulgation failed to result in vibrant financial markets. Russian stock exchanges were illiquid, shallow and characterised by virtual absence of initial public offerings (IPOs) until at least 2001. The explanation offered by the JSCA drafters was consistent with law matters thesis. As drafters have themselves admitted they underestimated the extent to which functioning law requires honest and competent courts, prosecutors and regulatory agencies to redress gross violations by firms' controllers (Black, Kraakman and Tarassova, 2000). In other words, by emphasising absence of adequate enforcement the Russian experiment in fact confirmed that law does matter for the development of equity markets.

Yet, the existing empirical evidence on the functioning of Russian enforcement institutions does not support this conclusion. Frye's survey of five hundred company managers in eight Russian cities revealed general satisfaction with how commercial courts handle business disputes (2003: 4). This is confirmed by research carried by Hendley et al, which illustrates high level of confidence expressed by the business community in the honesty and integrity of Russian judicial system (Hendley et al, 2001: 56 – 88). Similarly Hendrix's study shows considerable success rate experienced by foreign litigants in Russian courts thus refuting allegations of 'home-bias' (Hendrix, 2001: 94 – 120). The fact that commercial courts handle securities disputes on a regular basis (1834 in 1997, 3483 in 1999 and 2403 in 2000)

⁶ Part XI (sections 81 – 84) of the Act deals with specifically with self-dealing transactions.

and that Federal Securities Commission conducted 1318 enforcement proceeding in 1999 and 6000 in 2001 also support the surveys in denying dysfunction of enforcement processes in Russia (Pistor and Xu, 2005: 6 -7). In the light of these findings the Russian law's failure to bring about development of the stock market could be seen as evidence against the law matters thesis.

Thus there are strong counter arguments and evidence against law matters thesis, the failure of Russian law being but one among them. On the other hand, the fact that the law *did not* matter in UK or USA does not mean that it *could not* matter had it been there or that it *cannot* matter elsewhere. And as noted above Coffee has persuasively argued that private ordering can provide partial substitute to law until sufficient number of outside shareholders emerge to lobby for legal protections of their interests. In his view, the law then assumes central role in helping the market achieve its full potential (2002: 103). Similarly, although politics can explain absence of separation of ownership and control it is less clear why politics would discourage entrepreneurs from selling even minority stakes in their firms. Indeed socio-democratic countries like Sweden have developed vibrant stock exchanges concentrated share ownership notwithstanding (Angblad et al, 2001).⁷

In summary it is fair to suggest that the evidence on whether the law or other variables determine development of stock markets remains inconclusive thus leaving scope for further research. A comprehensive study of private enforcement of related party transaction rules in Russia offers one such research avenue and yet it has not been carried out to date. This thesis takes up the task.

1.2 Case Data and Research Methods

Russian judicial system is divided into three autonomous parts. The first two are the courts of general jurisdiction and the arbitrazh courts headed by the Supreme Court and the Supreme Arbitrazh Court (SAC) respectively. The third is the Constitutional Court with no lower instances subordinate courts. This section explains why the case data was collected from an arbitrazh rather than general jurisdiction courts and from the third tier arbitrazh court for the Moscow region (FAC) in particular.

⁷ For a commentary on Roe's politics thesis from the UK perspective see Cheffins, 2002.

At present, the competencies to try disputes are allocated to either the general jurisdiction or arbitrazh courts according to the subject matter of a dispute. Pursuant to article 27(1) of the Arbitrazh Procedure Code 2002⁸ (APC) arbitrazh courts have the competency over the disputes arising from the entrepreneurial and other economic activity. The term ‘economic activity’ is ambiguous and has caused problems in demarcating the competencies between the two judicial systems. Nevertheless, it is generally accepted that the arbitrazh courts exercise jurisdiction over the disputes arising from the companies legislation including the claims brought by the shareholders irrespective of their status (Dobrovolskii, 2006: 70). This is made clear by articles 33(1)(2) and 225.1(3) APC. The articles expressly state that the damages and invalidity claims brought by the members of a juridical person are subject to arbitrazh courts’ jurisdiction.⁹ Article 33(2) further states that disputes fall within arbitrazh courts’ jurisdiction irrespective of the legal status of the parties concerned: juridical persons, registered entrepreneurs, other organisations or individuals.

Prior to enactment of the APC 2002 the situation was different. Article 22(1) of the Arbitrazh Procedure Code 1995 restricted the competency of the arbitrazh courts to two types of claimants: the juridical persons and registered entrepreneurs. Disputes involving ordinary individuals fell under the competency of general jurisdiction courts, including claims brought by shareholders who were neither incorporated nor registered entrepreneurs. Cases surveyed in this thesis show that prior to 2002 the FAC heard no cases brought by such shareholders.

The thesis does not examine the general jurisdiction courts’ jurisprudence. Since the FAC had no jurisdiction over litigation involving physical persons prior to 2002, the analysis of the court’s jurisprudence for judicial bias during that period cannot exhaustively test the proposition that strong investor protection laws and their enforcement can facilitate stock markets’ development. This thesis would still leave open the possibility that general jurisdiction courts applied Part XI JSCA in a manner that would indicate judicial bias or incompetence.¹⁰ This is the thesis’s limitation. However, it is unlikely to be material for the following reasons.

⁸ As amended in July 2009 by Federal Law N 205-Φ3.

⁹ Prior to the 2009 amendment the relevant provision was article 33(1)(4) APC, which gave arbitrazh courts jurisdiction over disputes between shareholders and joint stock companies with the exception of disputes under labour legislation.

¹⁰ The author knows no study that examines the application of the JSCA by general jurisdiction courts in Russia. This is perhaps not surprising since the courts’ judgments have become more readily accessible only very recently with Russian electronic legal databases starting to store them.

First, the limitation would be significant if it prevented the shareholders who have sufficient incentives to actively monitor firms and pursue the section 84 actions where appropriate – the claimants who have a large enough shareholding to ensure that the increase in the value of their holding from pursuing the claim will outweigh the resources expended on the litigation – from gaining access to arbitrazh courts. This however is unlikely to be the case. The shareholders who are most likely to have the requisite incentives – professional institutional investors – will often be juridical persons and therefore, will be subject to the arbitrazh courts’ jurisdiction.

Second, the limitation would be significant only if the jurisdiction rule created a significant obstacle to the physical shareholders’ ability to gain access to the arbitrazh courts. This also is unlikely to be the case. Shareholders have a choice over the capacity in which they hold their shares. Physical shareholders could gain access to arbitrazh courts by either registering as entrepreneurs or, by holding their shares via a corporate entity. Either strategy would enable physical shareholders to bring themselves within the arbitrazh courts’ jurisdiction if they were intent on pursuing their actions there.

In summary, for the two reasons given above, the limitation in the case data is unlikely to materially affect its relevance to testing the relationship between investor protection laws, their enforcement, and stock markets’ development.

The structure of arbitrazh courts in Russia involves four levels of review. These are arbitrazh courts of the subjects of the Russian Federation (first instance); arbitrazh appeal courts (second/appellate instance); federal arbitrazh courts (third/ cassation instance) and the Supreme Arbitrazh Court (supervisory instance/ ‘nadzor’). The main difference between appellate and cassation instances is the scope of the review.¹¹ The former examines cases *de novo* whereas the latter is limited to legal error. Thus where the cassation court finds that the decisions of lower courts do not reflect the facts of the dispute or the documentary evidence it must direct the case to retrial.¹² The supervisory instance reviews cases on three grounds that a judgment in question potentially violates: uniformity of interpretation and application of the law; universally accepted human rights and freedoms according to norms and principles of international law; rights and lawful interests of an unidentified group of individuals and other

¹¹ The parties’ right to appeal to appellate and cassation courts are very similar. See articles 257 and 273 APC.

¹² Article 287(3) APC. Under the *de novo* review appellate courts can correct mistakes of fact and hence have no power to return the case to first instance for retrial (article 269 APC).

public interests.¹³ The review involves two stages. At the first stage the collegiate of three SAC judges determines whether to progress the case to the supervisory review, whether to bring a ‘protest’, on the basis of the application by one of the parties and against the grounds set out above. If the determination to bring a protest has been made the Presidium of the SAC then reviews the substance of the case.¹⁴ It is generally accepted that the supervisory instance is not a readily accessible process to review the judicial decisions in Russia.¹⁵

Table I below summarises official caseload statistics the SAC discloses on its website.¹⁶ It demonstrates well the SAC’s inaccessibility to appellants.

¹³ Article 304 APC.

¹⁴ Articles 292 – 308 APC.

¹⁵ European Court of Human Rights has refused to hold the analogous supervisory procedure in the general jurisdiction courts as the court of last resort, instead holding that the domestic remedies were exhausted at the cassation instance. See *Denisov v. Russia* (no. 33408/03, 6 May 2004); *Berdzenishvili v. Russia* (no. 31697/03, 29 January 2004).

¹⁶ SAC, 2006, *Table of Key Performance Indicators of Arbitrazh Courts of Russian Federation in 2002 – 2006* [Таблица Основных Показателей Работы Арбитражных Судов Российской Федерации в 2002 - 2006 гг.].

Available at http://www.arbitr.ru/_upimg/57605A349468E3993D142B3AD5AB4ABB_2006_vas-s_3.pdf. Accessed on 16 September 2013.

SAC, 2002, *Results of Work of Arbitrazh Courts RF in 1992-2001* [Результаты работы арбитражных судов РФ в 1992-2001 годах].

Available at <http://www.arbitr.ru/press-centr/news/totals/10anniversary/details.htm>. Accessed on 16 September 2013.

For ease of reference and due to periodic changes of the SAC webpage locations permanent hardcopies of the relevant pages are enclosed in Appendix 1, p.p. 7a – 12a.

Table I: Arbitrazh Courts' Caseload Data 1999 - 2006

Year	1999	2000	2001	2002	2003	2004	2005	2006	Total
Number of cases									
Heard by first instance courts	496739	539490	638287	697085	869355	1215627	1467368	1094849	7018800
Appealed to second instance courts	58530	67562	79957	84984	101729	118245	125882	136626	773515
Heard by second instance courts	42822	50450	61464	68769	84251	100484	109190	115832	633262
Appealed to third instance courts	34371	42828	55395	58719	75274	88679	94511	99109	548886
Heard by third instance courts	27718	35732	47028	51022	64339	77862	83867	87845	475413
Protest brought to the SAC	13484	15797	18167	18043	21830	19935	19472	19460	146188
Protests examined at preliminary stage	11556	14494	16867	18500	15153	15816	16172	16525	125083
Protests heard by the SAC Presidium	549	606	566	657	260	240	323	360	3561

Thus, according to the SAC statistics in Table I, between 1999 and 2006 the number of cases decided by the first instance arbitrazh courts in Russia exceeded seven million. Of these 9.02 percent (633,262 cases) were reviewed at the second instance; 6.77 percent (475,413 cases) at the third; 1.78 percent (125,083 cases) were examined at the first stage of the SAC's supervisory proceedings and only 0.05 percent (3,561 cases) were reviewed by the SAC Presidium. The figures show that the number of appeals heard by the second and third instances is not markedly different. The 475,413 cases heard at the third instance courts

equate to 75.1 percent of the 633,262 cases heard at the second instances. However, the second and third instances' figures stand in sharp contrast to the 3,561 cases (equivalent to 0.7 percent of the appeals heard by the third instance courts) that were reviewed by the SAC.

The figures indicate that, on the one hand, the parties that are inclined to appeal judgments of arbitrazh courts can and very often do take their cases to the third instance and, on the other hand, that the third instance courts are effectively the courts of last resort for the overwhelming majority of litigants. Thus, while the SAC judgments are undoubtedly an important source of judicial doctrine, and are of course discussed in this thesis, their relative infrequency renders them less than a useful proxy for evaluating judicial enforcement in Russia. For this reason the thesis focuses on the decisions made at the third instance. Support for the choice of focus can also be found from among commentators. For example, Vereshchagin (2007:13) explains:

'[t]he case law of these 10 circuit courts is of considerable importance and therefore is routinely monitored in legal periodicals. It is common understanding among practicing lawyers in Russia that the previous decisions of a relevant circuit court should be given careful consideration before engaging on a commercial dispute'.

The high volume of cases and the aim to systematically investigate changes in judicial doctrine over a relatively extensive period (1999 to 2006)¹⁷ restricted the scope of this study to one of the ten federal arbitrazh courts in Russia. The FAC for the Moscow region circuit was chosen due to the economic significance of the area subject to the court's jurisdiction. In 2007 27.5 percent of all enterprises in Russia were registered there representing the highest concentration of companies in the country.¹⁸ Logically, the highest concentration of companies ought to entail that the region's arbitrazh courts hear the largest number of related party transaction disputes.¹⁹ A search of Consultant+ (a well regarded Russian legal database used to construct the thesis's dataset) supported this expectation.

¹⁷ 1999 was the first year when the relevant cases were available within the database used in this thesis to construct the dataset. The dataset was assembled in early 2007. Therefore, 2006 was the last year of the surveyed cases.

¹⁸ Goskomstat, 2007, *Russian Statistical Yearbook* [Российский Статистический Ежегодник]. Available at http://www.gks.ru/bgd/regl/B07_13/IssWWW.exe/Stg/d03/12-03.htm. Accessed on 1 November 2013.

¹⁹ This is because both APC 1995 and APC 2002 allocate forum on the basis of the defendant's location (article 35 APC 2002; article 25 APC 1995).

Thus, as Consultant+ screen shots show,²⁰ the database contained 432,140 judgments issued by the 10 federal arbitrazh courts that fell within the date range 1 January 1999 – 31 December 2006.²¹ Of these, the highest number, 76,559 judgments representing 17.7 percent, belonged to the Moscow circuit.²² To construct the case dataset, the text of these judgments was searched using the term ‘ОБ АКЦИОНЕРНЫХ ОБЩЕСТВАХ’ – the JSCA’s title in Russian. The search, in other words, intended to pick up every judgment in the database that referred to the JSCA. There were 9,407 such judgments, of which the highest number, 2,001 judgments (21.3 percent), again came from the Moscow circuit.²³ The results were then filtered using a further word search, namely ‘81’, ‘82’, ‘83’, ‘84’, which are the numbers of the relevant sections in Part XI JSCA that deal with related party transactions. Moscow FAC again returned the highest number: 491 judgments.²⁴

Following this search, the 491 judgments were examined individually to remove from the dataset the judgments that featured JSCA but where the numbers 81, 82, 83, 84 referred to facts or provisions that were not sections 81, 82, 83, 84 JSCA or where the sections were not material to the substance of the disputes and judicial outcomes. Further 11 judgments that involved claims brought by prosecutors²⁵ and creditors²⁶ were excluded from the dataset.

²⁰ Appendix 1, p. 3a.

²¹ The 432,140 federal arbitrazh courts’ judgments in Consultant+ equate to 90.1 per cent of the 475,413 such judgments disclosed in the SAC official statistics. While caution should be exercised in drawing conclusions - the SAC does not disclose how the judgments figures are arrived at and hence there is no certainty that Consultant+ and SAC are measuring the same thing – at their face value the figures suggest that Consultant+ is a comprehensive database of federal arbitrazh courts’ judgments.

²² The second largest number, 71,025 judgments, was issued by the North-Western circuit FAC.

²³ Appendix 1, p. 4a. The second largest number, 1297 judgments, was from the Urals circuit FAC.

²⁴ Appendix 1, p.p. 5a, 6a. However, because the 491 judgments include judgments that do not involve related party transactions disputes under Part XI JSCA, the number provides only a very tentative indication that the Moscow circuit FAC might have heard the largest number of such disputes during the period reviewed in this thesis. A more robust comparison figure requires a judgment-by-judgment review and sorting of jurisprudence from all 10 federal circuits, a task beyond the scope of the thesis. As the following paragraphs explain such review was only undertaken with respect to the Moscow region FAC.

²⁵ *Постановление ФАС Московского округа от 9.03.00 по делу N. КГ-А41/782-00;*
Постановление ФАС Московского округа от 23.10.01 по делу N. КГ-А40/5957-01;
Постановление ФАС Московского округа от 31.01.02 по делу N. КГ-А40/4-02.

²⁶ *Постановление ФАС Московского округа от 6.06.01 по делу N. КГ-А40/2664-01;*
Постановление ФАС Московского округа от 7.06.01 по делу N. КГ-А40/2787-01;
Постановление ФАС Московского округа от 20.06.01 по делу N. КГ-А40/2961-01;
Постановление ФАС Московского округа от 21.06.01 по делу N. КГ-А40/2963-01;
Постановление ФАС Московского округа от 6.12.01 по делу N. КГ-А40/7132-01;
Постановление ФАС Московского округа от 17.03.03 по делу N. КГ-А40/1282-03;
Постановление ФАС Московского округа от 20.06.03 по делу N. КГ-А40/3784-03;
Постановление ФАС Московского округа от 7.10.03 по делу N. КГ-А40/7570-03.

After the sorting process was complete, 191 judgments remained in claims brought by companies and shareholders only.

In the course of this process it became apparent that occasionally disputes involved more than one FAC judgment. And whereas some judgments would be appealed and re-appealed to the court others would proceed as fresh proceedings. Hence, the judgments were reviewed closer to aggregate them into cases where appropriate. Two or more judgments were aggregated into one case where they involved identical parties and identical transaction. Thus, judgments were not aggregated where different claimants challenged the same transaction in several proceedings. The same approach was taken with judgments that involved the same parties but different transactions. This approach was chosen in the light of the thesis's objective to evaluate the FAC jurisprudence. Hence, judgments involving the same transaction might be decided against different claimants differently because of a particular procedural rule interpretation. And the same with the transactions – some, for example, may have been approved while others not. 170 cases remained when the aggregation process was completed.

The 170 cases form the dataset discussed in this thesis and are listed in Appendix 2. A unique case dataset number (CDN) has been assigned to each case listed in Appendix 2 for ease of reference. References to case data in the ensuing discussion are to these 170 cases listed in Appendix 2.²⁷

All 170 cases were brought under section 84(1) JSCA rescission remedy. There were no cases in the case data that contained claims for compensation under section 84(2) JSCA. The 170 cases were brought by companies that were party to the transactions and by the shareholders in a near even-split proportion of 49-to-51 percent (84 company cases; 86 shareholder cases).²⁸

²⁷ The date of the final judgment was used to date the aggregated cases. This was thought to be more useful than the date of the first judgment because this thesis focuses more on shifts in the FAC's jurisprudence than on the claimant litigation patterns. Of course, the discussion highlights the differences where they are material.

²⁸ As explained above the search also revealed a *de minimis* number of claims (11) brought by prosecutors and creditors which were not included in the dataset and were not examined in detail further save for where otherwise relevant to the discussion in the thesis.

In 120 cases (71 percent) the claimants were unsuccessful.²⁹ In 41 of these cases (34 percent) the judgments were based on the procedural grounds (the statute of limitations and contemporaneous ownership rule).³⁰ The remaining 66 percent of unsuccessful cases were decided on substantive grounds. The main substantive grounds concerned the claimants' failure to establish (i) a Part XI JSCA conflict of interest; (ii) a Part XI JSCA transaction; and (iii) a breach of Part XI JSCA approval process.³¹

For several reasons the ensuing analysis focuses only on the procedural grounds. First, the principal procedural rule, the statute of limitations, is the single most common ground for the unsuccessful case outcomes within the case dataset.³² Secondly, the operation of the statute has not been picked up in the debates and evaluations of the law matters thesis thus making for an underexplored and potentially fruitful field of academic enquiry. Thirdly, because the ground has not been under the spotlight it could provide an 'in the shadow' mechanism to reduce enforcement without affecting global rankings of Russia's investor protection regime. Finally, it is easier to construct a normative framework for applying rules, and to identify judicial deviations from the framework, with respect to the relatively straightforward procedural rules than with respect to more complex rules or standards such as for example those pertinent to the conflict of interest definition or the so called fairness review. Arguably, there is greater scope for opinions to divide over the appropriate interpretation of the rules or standards in the latter two examples.

In conclusion to this section a few words on methodology are in order. The thesis is a qualitative empirical study based on a theoretical and doctrinal analysis. It is empirical

²⁹ The success-failure descriptive statistics include the cases where retrial was the last known judicial outcome, with 'success' or 'failure' attributed to a case on the basis of whether the preceding instance's decision reversed by the FAC upheld (success) or invalidated (failure) a related party transaction. The judicial outcomes are listed in Column 4 of Appendix 2.

³⁰ Six judgments were decided against shareholders on the sole ground that the claimants had failed to establish a breach of their rights and interests. It has been suggested in the literature that the arbitrazh courts use the ground to deny shareholders' *locus standi* in claims under Part XI JSCA. From this perspective this 'rights and interests requirement' could also be considered a procedural rule, in which case there would be 47 unsuccessful cases decided on procedural grounds representing 39 percent of all unsuccessful cases. See Chapter 4 p.p. 151 for further discussion of the requirement.

³¹ Abbreviated summary grounds are listed in Column 5 of Appendix 2.

³² 35 unsuccessful cases were decided on this ground. Furthermore, the contemporaneous ownership rule may also be viewed as a rule functionally equivalent to the statute thus augmenting the number of cases to 41 (see Chapter 5 p.p. 202 – 216). The inability to establish a Part XI JSCA conflict of interest was the second most common ground (32 cases). Regarding the latter ground, however, it is fair to suggest that the relatively high number of cases is partially attributable to the breadth of the definition of conflict of interest in section 81, which is based on several sub-categories (see Chapter 2 p.p. 47 – 52).

because it is concerned with the judicial institutional capacity in Russia, which is an issue of fact. And as was shown above, the case data was systematically collected and organised on the basis of *ex ante* pre-defined criteria. The study is qualitative because in essence it interprets judicial texts. While descriptive statistics derived from the case data feature in the ensuing Chapters, it is the doctrinal analysis of the FAC judgments that is used to ‘test’ hypotheses elaborated below. Importantly, in this thesis ‘hypothesis testing’ is not the formal statistical hypothesis testing. The occasional borrowing of terms from statistics should not be read to mean that statistical significance testing was carried out – it was not. Rather the thesis involved testing in a more colloquial sense of the word: a systematic analysis of case data for evidence and counter-evidence of certain theoretical propositions. The hypothesis testing terminology and structure allowed for greater precision and objectivity in hypotheses formulation and for clearer demarcation of the normative-theoretical from the doctrinal-qualitative analyses. Given the complexity arising from the interplay of theoretical and jurisprudential propositions it was felt that the gains in clarity of the thesis’s structure and analysis outweighed any confusion over the thesis’s empirical research method, which it is hoped is addressed by the clarification in this paragraph.

Plan of the thesis

The remainder of the thesis is as follows. Chapter 2 assembles a judicial bias hypothesis – a more formal analytical framework to assess and evaluate the quality of the judgments. Chapter 3 then applies the framework to the judgments that had invoked procedural rules in company cases. Chapters 4 and 5 carry out the analogous task in relation to shareholders. Chapter 6 contains the thesis’s conclusion and implications of its findings.

CHAPTER 2

A JUDICIAL BIAS HYPOTHESIS

Introduction

The case data set out in Chapter 1 shows that more claims fail before the FAC than succeed. In itself, however, the figures alone say very little about the quality of the judgments. In the extreme, it is possible that all the dismissed cases were brought under the wrong legislation, for example. What is necessary then is a normative analytic framework against which the outcomes of the FAC decisions can be appraised. Of course, appraising the case data in this manner is difficult. Three interrelated concerns come immediately to mind. First, the normative yardstick must be capable of falsification (Ellickson, 1991: Ch. 11). In other words, it should be possible to identify and measure the criteria that make up the yardstick within the FAC judgments. Second, the yardstick must be objective so that the actual ‘measurements’ taken command a consensus among a hypothetical group of evaluators. For example, in a study of coloration in apples the assessors should be able to agree on which apples are red and which are green. Third, the yardstick must also command sufficient consensus as to its legitimacy. Within reason, it ought to be accepted by commentators as a valid normative framework for evaluating the FAC cases.

This Chapter pursues this task. For this purpose, it is helpful to formulate a ‘null hypothesis’ that for simplicity can be called the judicial bias hypothesis. The judicial bias hypothesis states that the FAC judges are biased, corrupt or incompetent and that these traits explain the outcomes in the case data. The substance of the Chapter develops and defends objective identifiable criteria the existence of which in the case data would challenge the hypothesis. The criteria are (i) higher order legal authority (which for the FAC includes primary and secondary legislation as well as the jurisprudence and edicts of the SAC); (ii) investor protection principle; (iii) Kaldor-Hicks efficiency. Forseeably it is the latter criterion that is

the most controversial and a large part of the Chapter argues that it is both appropriate and measurable.

The structure of the Chapter is as follows. Section 2.1 explains why the analytic framework is necessary. The answer it offers is the legal indeterminacy, meaning that the case data cannot be appraised on the basis of legislation and precedent alone. Section 2.2 explores whether the investor protection principle offers an adequate yardstick to evaluate the cases and concludes that while adequate it is insufficient. Section 2.3 turns to efficiency. It draws on the law and economics literature regarding judicial role in interpretation of incomplete contracts to identify the causes of contractual and by extension legislative incompleteness as well as the normative prescriptions on how the judges should fill the gaps in the incomplete contracts and law. In conclusion, the hypothesis is formulated.

2.1 The Problem

A helpful starting point is Pistor and Xu's paper, which is implicit in its criticism of the JSCA drafter's self-enforcing model. Pistor and Xu observe that 'while [institutional reform] is a difficult task and will take time to accomplish, it cannot be easily circumvented by writing law that limits the role of courts in this crucial area of the law' (2002: 7). The authors argue that the inherent incompleteness of the law, the impossibility to design rules that cover all future contingencies, requires legislators to allocate residual law making powers to courts or regulators if the law is to act as an effective deterrence device. The idea of the incompleteness of the law, or legal indeterminacy, is not new and is familiar to legal scholars in the common law jurisdictions and in Russia.¹ For the present purposes its relevance resides with the fact that the FAC judgments in the case data are likely to turn on the issues where the legislation or a superior legal precedent does not provide an unequivocal answer. In such situations the judges are acting as law-makers / legislative gap fillers (Vereschagin, 2007: 60-64) and the non FAC judge made law is unavailable as an objective yardstick to evaluate the FAC adjudication. Evaluating the FAC's adjudication against the FAC's law making, which in the indeterminate law circumstances is the same thing, would foreseeably fail to command academic acceptance as a legitimate yardstick. Other, normative standards are necessary.

¹ For an examination and analysis of the Hart – Dworkin debate on this issue in the Russian context see Vereschagin, 2007: 39-58.

On Pistor and Xu's assessment courts, for a number of reasons, are preferable to regulators in the task of completing incomplete law (2002: 7). However, it is one thing to suggest that the courts should or *de facto* do have residual law making powers, it is quite another to suggest how they should discharge these powers. This point is crucial because when commentators evaluate adjudication *ex post* the evaluation is informed by their belief as to how the cases should have been decided. A common criticism, particularly in the circumstances where legislation does not provide a clear answer, is that the courts are unduly formalistic, do not care for the real rights and wrongs underlying the dispute and defer to the interests of strong parties (Enriques, 2003). However, such criticisms presume, first, that the 'real' rights and wrongs are easily identifiable and secondly that they can be cured by purposive interpretation, neither of which is necessarily self-evident as this Chapter attempts to illustrate. More importantly such critique masks what is really at issue, the disagreement as to the scope of application of a particular rule between the court and the commentator. The presence of a rule does not *by itself* warrant its extension by the judges in all the circumstances. Failure by a judge to interpret law expansively should not necessarily be an indication of 'bad' enforcement. Instead the choice between 'narrow' and 'expansive' interpretation should be defended on its merits in the context of the dispute being tried.² In other words what is often missing in recent commentary is an examination of when and how should the judges fill the gaps in legislation.

The point is not an exercise in metaphysics. It has a considerable practical significance to the subject matter of this thesis. What do commentators mean when they state that 'existing case law from Russia reveals that courts are still struggling with recognizing conflict-of-interest situations' (Pistor and Xu, 2003: 94); or that there is 'insufficient development of the general notion of 'conflict of interest' in Russian law' (Back et al 2006, English versions: 54); other than that the commentators would have recognised the conflict where the judges had not?

An example can help demonstrate the argument presented in this thesis. In March 2001 the SAC issued Information Letter No.62 reviewing a number of related party transaction cases. Paragraph 19 concerned a dispute between InvestCredit (the IC) and Russian Financial Corporation (the RFC) where the court reversed lower decisions and held that the approvals

² Indeed, even the authors arguing against formalist interpretations admit that in certain circumstances formalism may be 'good' and should be followed by the judges (Enriques, 2003: 9). Such statements would be unnecessary if it is accepted that the dispute is over the applicability of a rule in a given situation.

requirements do not apply to transactions that, pursuant to other legislation, are mandatory for a firm. The case proved to be the more controversial aspect of the Information Letter with the commentators. In particular, it has been cited to suggest that Russian courts are ‘struggling with recognizing conflict of interest situations’ (Pistor and Xu, 2002: 27, 28).

The facts of the case were as follows. The RFC held one third of the IC’s voting share capital and both firms had a common managing director. The firms were also in a bank-client relationship, RFC being the client. In September 1998 the RFC instructed the IC to convert the roubles it held with the IC into 460000 US dollars. The IC used the dollars held in its own currency portfolio for the purpose. Following the transaction the IC retained 296000 under an inter-banking loan agreement repayable in December 1998. None of the transactions were approved under the related party provisions under Part XI JSCA. When the IC failed to repay the loan the RFC brought an enforcement claim. In defence the IC argued that the loans were invalid because the related party transactions approvals were not obtained. Additionally, the IC brought separate proceedings against the RFC to hold the purchase of dollars invalid on the same grounds.

IC’s motivation appears to be clear. It would have to repay the principal in dollars regardless of whether the loans are held invalid.³ However, pursuant to the restitution order, invalidity of the currency purchases would lead to the IC returning roubles to the RFC in exchange for the dollars. Currency transactions restitution could then be set-off against the loan’s principal. In effect the IC would end up repaying the principal in roubles. Given the change in the rouble-dollar exchange rate from 9-1 on the date of the transactions to 18-1, due to the 1998 financial crisis that had happened in the interim, on the repayment date the IC would end up repaying only half the principal amount. Furthermore, the RFC would also have to bear the losses on the currency exchanged in excess of the loan amount.

Three separate trials were held for each foreign exchange transaction. In two cases transactions were held invalid at all three instances of the commercial court. In the third case first instance and appellate courts found transaction valid but the decisions were reversed at the third instance. The SAC reversed all three decisions and sent them for a retrial. The IC dropped the claims before the retrial.⁴

³ If the loans are held invalid they would still have to be restituted.

⁴ *Постановление ФАС Московского округа от 26.07.99 по делу N. КГ-А40/2274-99* CDN7; *Постановление ФАС Московского округа от 4.08.99 по делу N. КГ-А40/2383-99* CDN9;

Currency conversion was carried out at the market exchange rate posted by the Central Bank of Russia. Therefore, the transactions were at arm's-length price and no expropriation was taking place. The interests of minority shareholders in the IC were unaffected⁵ and the case had nothing to do with protecting outside investors. The SAC's judgment is clear in what influenced its decision, *'[t]he losses sustained by a bank in a foreign currency sale-purchase transaction due to subsequent change in the price of the currency in relation to rouble cannot be imposed on the client who provided sufficient consideration to be converted back into the currency practically to the same amount at that moment in time. Missing this opportunity by the bank, which under legislation has the right to purchase foreign currency without restrictions, is not caused by the actions of the counterparty in these types of transactions and cannot be taken as the consequence of such actions.'*⁶ In other words the counterparty, the RFC, cannot be held responsible for IC's failure to hedge its exposure to the rouble. To require the RFC to bear the IC's loss on rouble devaluation would be unfair because the RFC had no influence over the IC's foreign currencies portfolio.

It is of course possible that the court may have struggled to recognise the conflict of interest. But it is also possible that the court was arguably motivated by the injustice that the strict no conflicts policy would create to the counterparty. And it is notable, that the court referred to the IC being in the best position to avoid the loss. Perhaps, had the court the freedom to review the transactions' merits it could have easily concluded that, despite the conflict of interest, the transactions were substantively fair and therefore valid.

Yet, in the absence of the merits review the SAC chose a different route to reach its conclusions. Under article 845(3) of the Russian Civil Code banks cannot impose restrictions, in addition to those stipulated by law or the terms of the bank account agreement, on the use of the clients' funds. If a client wishes to lawfully purchase foreign currency and provides roubles for the purpose the bank has no right to refuse to execute the order. Since the bank had no right to refuse the transaction, neither did its board of directors, nor its general meeting. As the SAC put it, the approval requirements in article 83 of the JSCA 'apply to those transactions which the organs of a company have a right not to permit, but not

Постановление ФАС Московского округа от 4.08.99 по делу N. КГ-А40/2531-99 CDN10;
Постановление Президиума ВАС РФ от 19.09.00 No.1873/00.

⁵ It could be argued that where markets are volatile dollars are better assets to hold than roubles. This argument however does not apply in this case because the IC was free to purchase more dollars with the RFC's roubles to maintain its original dollar position.

⁶ *Постановление Президиума ВАС РФ от 19.09.00 No.1873/00.*

to those transactions which are mandatory for companies pursuant to requirements of legislation or other regulations'. The statement to this effect appeared six months later as a general proposition for applying related party transactions rules in paragraph 19 of Information Letter No.62. Perhaps, the court was wrong to create a precedent that exempted mandatory transactions from Part XI JSCA. But also perhaps, the court might have been concerned not to create a precedent that exempted all transactions that are substantively fair from the Part XI JSCA. It is possible the court was acting in the outside investors' interests after all.

In short, legal provisions are often incomplete leaving judges with a significant measure of discretion in applying law to facts. How judges carry out that task can lead to disagreements as the above example demonstrates. Hence the need for criteria that has objective features and on which commentators could agree.

2.2 Investor Protection

The most straightforward approach for judges in their gap-filling role is to interpret ambiguities in accordance with a principle or purpose of the legislation. And this would then make for an objective and easily measurable yardstick. If investor protection, for example, could provide adequate guidance to the courts it could also act as a yardstick to evaluate judicial decisions. The enquiry would simply involve an examination of the judicial deference to the claimants' interests in the penumbral cases.

Thus, in the Anglo-American jurisprudence there is an interpretative approach rooted in the fiduciary law. As Coffee explains, 'the justification for judicial intervention is essentially grounded on moral considerations: once managers or directors are deemed to be trustees, it follows that they must subordinate their self-interest to that of their beneficiaries, the shareholders. This approach then allows courts to articulate mandatory norms of conduct, which govern most intracorporate relationships, whether or not the actors themselves have such expectations or wish them to apply' (Coffee, 1989: 1624).

To be sure, there is no concept of fiduciary relations in Russian legislation (Black et al, 2006b: English version: 25). But one does not have to look far to obtain an alternative. The protection of outside investors was an openly declared goal by the JSCA drafters (Black, Kraakman and Tarassova, 1998: 23-26). A more recent Report prepared by a number of

American and European academics for the Russian Centre for Capital Market Development and the Russian Federal Service on the Securities Market reiterates this policy goal in its introduction,

‘For Russian companies to receive full trust from foreign investors adequate legal regulation is necessary particularly in the sphere of conflict of interest transactions’ (Black et al, 2006b: Russian version: 1).

Thus, a court faced with an alleged breach of related party transaction rules in the circumstances where the application of the rules is unclear should read the law expansively in favour of minority shareholders, the investors. In other words, the purposive interpretation of the law by the courts can remedy the deficiencies in legislation.

In fact, the focus on investor protection as a guiding principle for adjudicating related party transactions disputes has an advantage over the fiduciary principle at least for the proponents of the approach. It extends to situations involving majority shareholders who do not hold official posts with the firms, the situations where Anglo-American and some European jurisdictions have had some difficulty since the majority shareholders are not *strictu sensu* fiduciaries, provided their involvement with firms is limited to the shareholding (Black et al 2006b: English version: 71-77). Since the investor protection principle attaches to the status of the potential ‘victims’ (the investors) rather than to the status of the ‘expropriator’ (fiduciaries, managers, controlling shareholders) its scope of application is broader.

There are a number of objections to the use of investor protection as the sole rationale to guide the courts and to evaluate their judgments against. First, the strength of the investor protection principle rests on the proposition that it assists the development of stock markets. This proposition, as indicated in Chapter 1, has been subject to academic criticism. And if the principle cannot be supported by extrinsic evidence the argument becomes tautological.

The second objection is that the JSCA drafters themselves sought to circumscribe the application of the related party transaction rules:

‘This [section 84] invites a court to declare a transaction invalid, even when the other party to the transaction has entered into the transaction in good faith, not knowing of the violation of the approval requirement contained in article 83. For conflict-of-interest transactions, as for major transactions, it is important to protect the rights of third parties. This could be achieved by treating the conflict-of-interest rules as part of the company’s internal

governance, rather than as affecting the validity of the company's transactions with third persons.

In our judgment, invalidation is an appropriate remedy for violation of the conflict-of-interest rules only when a conflict-of-interest transaction is concluded directly with an interested person, his close relative, or a juridical person that is 100% owned by an interested person, or with another person who knew or should have known of the violation of the conflict-of-interest rules' (Black, Kraakman and Tarassova: 1998: 461).

As the quote demonstrates, the drafters' proposal is significantly narrower than the JSCA rules in force during the surveyed period. Given the drafters' preference for a significantly narrower set of related party transactions rules it may be inferred they would opt for a judicial practice that resolves ambiguities in the rules in a more constrained manner than would otherwise follow from an unequivocal commitment to the investor protection principle. In other words it is questionable whether the investor protection, albeit dominant, was *the sole* guiding principle informing Russian companies legislation. This renders purposive interpretation of the law in favour of investors difficult.

Thus, the quote's reference to the importance of protecting third parties suggests the third objection to strict adherence to the investor protection principle in the related party transactions adjudication. Investor protection and regulation of conflicts of interest is not the only objective company law and law more generally pursues. As the quote suggests, the conflict of interest regulation conflicts with the freedom of contract and the operation of the markets for goods, service and finance. As will become apparent from Chapter 3, protection of third parties is an important consideration in evaluating the FAC's adjudication in this thesis.

But the point is broader: conceivably policies corporate law pursues may also end up in conflict in a dispute. For example, one essential function of company law, the facilitation of affirmative asset partitioning, may conflict with the strict application of related party transaction rules that would follow the strong adherence to the investor protection principle. The function is described as essential because it cannot be provided for by contract, unlike the fiduciary duties (Hansmann and Kraakman, 2000). The affirmative asset partitioning, the protection of firms' assets from shareholders' creditors, reduces credit costs and protects firms' going concern value. In doing so it also eliminates the need to monitor shareholders' wealth and thereby promotes free transferability of shares. The importance of free

transferability of shares to stock market development is indisputable: if one could not sell shares at will, there would be no market for shares. In other words where investor protection comes into conflict with affirmative asset partitioning preference of the former principle in the application of the related party transaction rules could turn out to the detriment of the stock market. Arguably it would be very difficult for a court to ascertain a guiding principle to steer its decision in a dispute where a shareholder's liquidator seeks to unwind transfer of funds in exchange for shares in a new company several years after the transfer took place.

In sum, although the investor protection is straightforward in application and in measurement it has significant limitations. The key obstacle is how to resolve disputes where other policy objectives conflict with the investor protection principle. What should guide the inevitable tradeoffs?

2.3 Welfare Maximisation

When tradeoffs are unavoidable, there is an avenue to reduce conflicting policies to a common denominator. Law and economics literature offers one such common denominator (Diver, 1993: 72). Law and economics scholars posit that the courts should supply efficient 'gap filler' rules when confronted with an incomplete contract. The rules are efficient when they lead to the net aggregate gains in the welfare of the parties', which in the context of corporate law are accepted to be the investors (Cheffins, 1997: 133; Schuster, 2010: 21) – controlling inside and minority outside shareholders. Norms will maximise the parties joint welfare when they minimise the sum of deadweight losses – losses from failing to exploit gains from trade and costs incurred in redistributing wealth – and the transaction costs incurred in minimising the deadweight losses (Ellickson, 1991: Chs. 10 and 11). In the related party transactions context, the aggregate welfare maximising rules are the rules that ensure the realisation of the value creating transactions and the avoidance of value diversion while reducing the sum of the bonding, monitoring and enforcement costs (Goshen, 2003: 401, 415-421).

The choice of efficiency as a normative criterion should not be controversial for the JSCA drafters themselves thought that the 'efficiency goal of maximizing the company's value to investors remains ... the principal function of company law' (Black, Kraakman and Tarassova, 1998: 23). The difficulty, however, resides with the fact that ultimately the balance between the costs and benefits of a particular rule requires empirical evidence on the

quantifiable net gains or losses to the parties, which is difficult, perhaps impossible, to obtain (Brudney, 1997). The existing empirical studies that either focus on the impact of the individual measures on firm valuations or that conduct cross country private benefit of control valuations have often been criticised on methodological and epistemological grounds (Dammann, 2007: 699 – 705; Schuster, 2010: 19). The latter studies, for example, calculate the average private benefits of control across different jurisdictions by measuring the difference in value between voting and non-voting stock in firms with dual-class shareholding structure or the premium acquirers' pay for the controlling block (Nenova, 2003; Dyck and Zingales, 2004). Even assuming that the differences in control premia these studies identify reflect differences in the legal, rather than say social, norms; to a judge attempting to apply a statute of limitations, and to a scholar attempting to establish whether that application was efficient, their practical utility is arguably limited.

The next two sections consider how to break the impasse. The first, examines Goshen's efficiency framework for regulating relating party transactions that seemingly escapes the difficult empirical evaluations (Goshen, 2003). The second, looks at the so-called hypothetical bargaining model.

2.3.1 Goshen's efficiency framework

Goshen's framework evaluates the efficiency of two of the more common and contrasting approaches to regulating relating party transactions: the majority of the disinterested minority approval requirement and the fairness test. Under the former approach related party transactions are invalid unless they receive the consent of the majority of the non-conflicted shareholders. Under the latter approach, unapproved related party transactions can escape invalidity provided they are substantively fair (Goshen, 2003: 402, 403). The framework holds an efficient approach to be the one that ensures the realisation of the value creating transactions and the avoidance of value diversion while reducing the sum of the transaction costs, which tend to be greater under the 'majority of minority' approval because routine recourse to the general meeting is necessary, and the adjudication costs, which tend to be greater under the fairness test because routine recourse to courts will be necessary (401, 415-421). To overcome the difficult empirical balancing of the costs and benefits of the two approaches Goshen relies on two heuristic factors, which he argues can tilt the efficiency balance in favour of one approach or the other.

The two factors are the likely distribution of transactions in terms of value creation and value diversion and the judicial institutional capacity to operate the fairness test in a jurisdiction (415, 417, 420). The outcome of Goshen's efficiency analysis is that the majority of minority approval will be efficient, and the fairness test inefficient, in jurisdictions where the value diverting transactions prevail over the value creating transactions because the losses from the forgone value creating transactions and the high transaction costs will be outweighed by the savings in the adjudication costs and the smaller losses from the value diverting transactions; and, regardless of the distribution, where the judiciary does not have the necessary institutional capacity to effectively determine whether a transaction is fair, that is whether the transaction was completed at, above, or below its 'correct' value (417, 418, 420).

Five additional factors aid Goshen's assessment: the existence of market for corporate control; the efficiency of capital markets; the presence of sophisticated investors; corporate reputation; and the frequency of the related party transactions. The first four factors, more precisely their presence or absence, help determine the likely distribution of the transactions, albeit Goshen does not state so expressly. Throughout the analysis these 'market' factors are alluded to to gauge the degree of protection accorded to the minority shareholders, in other words, to ascertain the likely prevalence of the overreaching self-dealing transactions.⁷ The relevance of the frequency of the transactions is uncertain and Goshen reaches no clear conclusion on this point (413, 414). This is perhaps not surprising since high frequency of related party transactions in a jurisdiction will increase the transactions costs under the majority of minority approach because a more frequent recourse to the general meeting will be necessary, and increase the adjudication costs under the fairness test by requiring a more frequent recourse to the courts, and vice versa.

The framework does not bode well for the efficiency of the fairness review in Russia, an emerging market jurisdiction with the concentrated structure of corporate ownership where the market factors that could reduce the incidence of value diverting transactions are lacking or underdeveloped. Similarly, the judicial institutional capacity in Russia has been doubted, albeit this thesis is seeking to investigate this. Indeed, Goshen's analysis closely reflects the

⁷ 'When the market for corporate control is effective, there are few cases of exploitation of minority shareholders' (422); 'the capital market should protect the minority' (423); 'the presence of sophisticated investors deters the occurrence of exploitation through self-dealing' (424); 'reputation ... reduces the prevalence of self-dealing transactions' (425).

arguments given by the JSCA drafters⁸ for enacting the law that reduces the reliance on judiciary in Russia so much so that he cites their work in support of his analysis (415).

However, Goshen's framework does not fully escape the difficult issue of the empirics. Both the distribution of transactions and judicial institutional capacity, however the latter is defined, are empirical matters. The shortcoming may not wholly undermine the framework's usefulness, but it certainly makes the framework inadequate for the purpose of formulating a falsifiable hypothesis to test private enforcement by the courts in Russia. Absent *a priori* empirical evidence on the transactions' distribution or the judicial capacity it is impossible to construct such hypothesis using Goshen's analysis.

Thus, as far as the distribution of transactions is concerned, it is plausible that the presence or absence of the market factors can indicate the likely incidence of value diverting transactions. Yet, on Goshen's analysis, these factors tell very little, if anything, regarding the incidence of value creating transactions and whether or not such transactions are likely to be more prevalent than the value diverting transactions. Indeed, the framework's reliance on these factors only begs the question whether in any jurisdiction where the concentrated corporate ownership structure, inter-locking directorships and cross-shareholdings dominate, allowing courts to review related party transactions on their merits can ever be efficient.

In fact, it is equally possible to plausibly argue that the absence of the market factors can indicate a high incidence of value creating related party transactions. For example, most concentrated ownership jurisdictions fall within what the Varieties of Capitalism literature describes as the Coordinated Market Economies where firms depend more heavily on non-market relationships to coordinate their endeavours, which 'entail more extensive relational or incomplete contracting, network monitoring based on exchange of private information inside networks, and more reliance on collaborative, as opposed to competitive, relationships to build the competencies of the firm' (Hall and Soskice, 2001: 8, 1-68; Bratton and McCahery, 1999: 229-233; Dignam and Galanis, 2009: 46, 160-161). In jurisdictions where firms predominantly coordinate their activities, that is generate value, outside competitive markets, it is possible to reasonably maintain that many related party transactions – prototypical examples of non-market economic coordination – will be value creating.

⁸ Black, Kraakman and Tarassova, 1998, citing the absence of market factors (15) and weak judiciary (28).

The argument is stronger still in the context of the emerging market jurisdictions such as Russia where it is conceivable the firms would face considerable difficulties in coordinating and building their competences on the basis of the competitive market arrangements. These, by definition, are only emerging. Empirical studies support this proposition: in jurisdictions where the financial and product markets are ‘thin’ firms build and maintain relationships with their trading partners to mitigate information asymmetries (McMillan and Woodruff, 2002: 159-165). In other words, interlocking directorships and cross-shareholdings, the circumstances that attract the application of Part XI JSCA, in Russia can also be explained as a strategic business response to ‘weak’ market institutions.⁹ It follows the absence of market factors can be as much an indication of the high incidence of value creating related party transactions as of the high incidence of value diverting transactions. Perhaps, the absence of these factors could credibly indicate a high frequency of related party transactions, yet as noted above, the frequency alone cannot swing the cost-benefit assessment in favour of either the majority or the minority or the fairness test approaches: the frequency increases both the transaction costs and the adjudication costs.

In sum, without empirical evidence, the question of the transactions’ distribution invites as much speculation as the comparative assessment of net gains or losses to the parties’ welfare under the majority or minority versus the fairness test approaches; the speculation that is scarcely made more conclusive by the existence or absence of the market factors. If it is impossible to ascertain *a priori* the type of the related party transactions that are likely to be prevalent in Russia, it is also impossible to determine the efficiency implications of the fairness test by reference to the transactions’ likely distribution and, therefore, to formulate a hypothesis to test outcomes in the case data.

The judicial institutional capacity is an equally problematic indicator of the likely welfare implications of the two approaches. It gives rise to analytical as well as empirical concerns. Empirical data on, and objective criteria for evaluating, judicial capacity are necessary to reach a determination whether courts in a jurisdiction can ‘operate’ a fairness test based approach. As was shown in Chapter 1 of this thesis, academic opinion on the capability of Russian judges is contradictory. Albeit the empirical studies suggest the judiciary is,

⁹ For example, Gray and Hendley’s study of a typical Russian enterprise found that the outside directors were appointed for ‘strategic business reasons’ and that many transactions were concluded without shareholder approval but this was not to say that they were not in the interest of the company, concluding that ‘perhaps they [were]’ (Gray and Hendley, 1997:158, 159).

according to the different criteria and methods the studies adopt, satisfactory, none have examined the related party transactions adjudication. Herein lies the key difficulty of using the judicial capacity criterion for the purpose of this thesis: to assess the judicial capacity by evaluating the adjudication against a falsifiable hypothesis. The inevitable circularity that would ensue is apparent. In relation to the fairness test, the hypothesis will be rejected if it can be shown that the FAC's jurisprudence is efficient. Yet, the jurisprudence can only be efficient if it is determined *a priori* that the judiciary is, in some way, capable, i.e. by *a priori* rejection of the hypothesis. The circularity makes it impossible to formulate the hypothesis on the basis of the judicial institutional capacity as an indicator of the likely (in)efficiency of the fairness test in Russia.

2.3.2 Hypothetical bargaining model

There is a solution to the above difficulties, albeit one that does not command a unanimous approval of the corporate law scholars.¹⁰ When confronted with incomplete contracts the courts should supply the gap filler terms that the transactors would have themselves selected had they possessed full information and put their mind to the unforeseen issue. Since rational parties dealing at arm's length would not ordinarily enter into agreements that would make them worse off, by focusing on what they would have bargained for the courts would be attempting 'to mimic the results which perfectly functioning markets would yield' (Cheffins, 1997: 129, Ch. 6).

Thus, in the context of the fiduciary duties it has been argued that '[s]ocially optimal fiduciary rules approximate the bargain that investors and managers would have reached if they could have bargained (and enforced their agreements) at no cost' (Easterbrook and Fischel, 1991: 92).

To be sure, the hypothetical bargain cannot be a panacea for the efficiency-minded judges and also for those trying to evaluate their decisions. Applying the hypothetical bargaining

¹⁰ In the absence of empirical evidence, Brudney for example maintains, it is impossible to establish whether the strict no conflicts or the fairness review approach will be the welfare maximising norm, 'the question is not answered by reference to 'contract' as a relevant process, by antiseptic economic models, or by speculation about how rational wealth-maximizing actors in them (even when organized as institutional owners) would perform, any better than intuitions about (and experience with) the acquisitive behaviour of management [and controlling shareholders]' (Brudney, 1997: 617, 621, 635-640).

model, as Cheffins explains, ‘involves thinking about what rational transactors would contract for if they had perfect information, did not face significant transaction costs, and could be fully confident that the agreements reached would be performed as arranged’ (1997: 264). No doubt, to expect an FAC judge to be aware of what applying the model entails is a tall order. To expect the judge to apply it is perhaps fanciful. For example, in *Jordan v. Duff & Phelps* 815 F.2d 429 (7th Circuit, 1987), Judges Easterbrook and Posner, both strong proponents of the model, delivered opposing opinions. The former Judge implied fiduciary duty to the contractual relationship disputed, whereas the latter did not (Ayres and Gertner, 1989: 119; Coffee, 1989: 1680, 1681). If eminent professors of law and economics struggle to reach the same outcome using the same method, it may be unrealistic to expect the FAC judges to apply the model and deliver welfare maximising outcomes. The prospect of formulating a hypothesis to assess the case data may hence be futile.

Three reasons suggest that the problem is not intractable. First, the problems that come to divide the parties may appear clearer in retrospect, enabling courts to determine what the parties would have agreed had they contemplated the problem (Schwartz, 1992: 281). And the same has been said about the corporate law, ‘[f]rom its *ex post* perspective, a court can more easily determine if opportunistic advantage has been taken of the minority’ (Coffee, 1989: 1622). Secondly, efficient interpretations of incomplete legal provisions are often intuitive. Thus, Posner has argued that many common law doctrines, and there is not a priori reason why this observation should be limited to the common law rather than any judge made law, are economically sensible but not economically subtle. ‘They are commonsensical’, he explains, ‘their articulation in economic terms is beyond the capacity of most judges and lawyers, but their intuition is not’ (Posner, 1998a: 274, 275). Thirdly, as should become clearer by the end of this Chapter, the hypothetical bargaining model is a useful analytic tool only in relation to the transaction costs sources of incompleteness. With respect to the problems of verifiability and information asymmetries different, and perhaps less subtle, welfare maximisation considerations apply.

One final criticism of the hypothetical bargaining ought to be mentioned before moving on to discuss the causes of, and the efficient judicial responses to, the contractual and legislative incompleteness. The hypothetical bargaining model and aggregate welfare maximisation are analytic constructs premised on Kaldor-Hicks efficiency. As such the efficiency imperative is net gains to the parties irrespective of how those gains (or losses) are distributed. However, as Coffee put it, ‘*nothing that we know about the real world suggests that*

individuals are actually so risk neutral as to behave in a fashion that is indifferent to distribution of gains and losses. If in fact parties do not bargain only to reach the efficient outcome, then courts would ignore important issues of distributive fairness if they performed their gap-filling role by falsely assuming that the parties desired only to maximise aggregate wealth' (1989: 1623).

Not to diminish the significance of this point, and acknowledging that the question of distribution and economics divides opinion,¹¹ it is sufficient to note that distribution is an extraneous consideration to the task pursued in this thesis. It is not a purpose pursued here to establish the primacy of the efficiency over the distribution or vice versa. Rather the task is more modest, to appraise the FAC jurisprudence against objective criteria to test a hypothesis of judicial bias or incompetence. Aggregate welfare is used as a normative yardstick for this purpose only. Efficient case outcomes would be inconsistent with the judicial bias hypothesis. Whether these judgments are then good or bad against some other objective or subjective criteria is a separate question not pursued in this thesis.

Furthermore, as already noted above, the JSCA drafters thought that the efficiency goal remained the principal function of company law in emerging economies (Black, Kraakman and Tarassova, 1998: 23). It would seem sensible, therefore, to use efficiency as one of the normative yardsticks for the assessment. Of course it is also hoped that the supporters of the view that corporate law should embrace distributional goals would find the thesis informative. After all, efficiency must be a more palatable institutional attribute than bias, corruption or incompetence.

2.3.3 Transaction Costs

Thus, the law and economics literature identified three particular transaction cost causes of incomplete contracts. The first concerns linguistic limitations – parties may be unable to describe future contingencies with sufficient precision and consequently may leave contract terms ambiguous or vague (Schwartz and Scott, 2003: 570-594; Hart and Moore, 1998: 757; Anderlini and Felli, 1994). In contrast, the next two causes arise when parties fail to appreciate, rather than describe, future contingencies. This may be due to the bounded

¹¹ Testament to this is that almost every law and economics text considers the issue Cheffins, 1997: 142; Posner, 1998a: 495; Cooter and Ulen, 2003: 7.

rationality of the individuals or the inherent uncertainty of the future. The second cause occurs when parties inadvertently overlook a future contingency and the third cause where, regardless of the parties' efforts, it is impossible for them to perfectly anticipate every future contingency and provide for it contractually (MacNeil, 2001: 113, 114). Doubtless, similar problems arise in legislative drafting. As Pistor and Xu have aptly put it, *'[i]f contractual parties cannot write complete contracts, lawmakers should be even less able to write complete statutory law. In fact, to write a complete law, lawmakers would need not only unlimited foresight, but should be blessed with unbounded rationality. They would need to be able to anticipate the impact of the rules they make on all potential parties concerned and write rules that can achieve the best results from a social welfare perspective'* (2002: 9).

The three causes are expressed as the transaction costs causes of incompleteness in the literature (Ayres and Gertner, 1989: 92; Schwartz, 1992: 278, 279) because they can be understood in terms of the costs of contracting (or law making) – researching the effects and probability of a contingency; and negotiating and drafting a particular contractual solution (or a legal edict), which may outweigh the private gains from the solution to the parties (or the social welfare gains) – and this is how they will be referred to in this thesis.

When transaction costs are the sole cause of incompleteness, the law and economics approach posits that the courts should supply the gap filler rules formulated in accordance with hypothetical bargain (Cheffins, 1997: 133).

2.3.4 Verifiability

Another reason that may lead contractual parties to leave certain provisions outside their agreement that has been documented in the law and economics concerns information. Thus, as Schwartz has argued, contractual incompleteness often occurs where the information on which a contractual term would have to be conditioned is unobservable or unverifiable (Schwartz, 1992). Information is unobservable if a party cannot observe it. Information is observable but not verifiable where a party can observe it but cannot verify information's existence to a third party such as a court. Where information is either unobservable or unverifiable the issue is described as noncontractible. In these circumstances the parties *choose* an incomplete contract *ex ante* where compliance with a term that would make contract more complete cannot be observed or verified because the more complete contract

would create an incentive for strategic behaviour *ex post* (Schwartz, 1992: 279, 280; Schwartz and Scott, 2003: 605-606). For example, the scarceness of terms in long-term supply of goods contracts that condition prices on seller's costs has been explained on the ground that the sellers' production costs are usually unobservable to the buyers. Such terms would create an incentive for the seller to argue that its costs have increased, and for the buyer to argue that the seller's costs have been manipulated (Schwartz, 1992: 280; Bernstein, 1996: 1791-1796). As Schwartz put it, '*certain contracts are incomplete not because the parties overlooked or failed to understand the issue that came to divide them but because they are unwilling to bear the strategic-behaviour risk that a complete contract would create*' (1992: 273).

The law and economics literature maintains that courts behave passively when confronted with incomplete contracts that are incomplete due to the unobservable or observable but unverifiable information. The problem, as Whincop put it, 'renders redundant the use of legal rules to fill these 'gaps', since verification problem equally afflicts them' (Whincop, 2001: 35). In other words, the courts cannot better the parties at completing the contract. Indeed, the passivity would accord with the law and economics' hypothetical bargain. The contracts are incomplete because parties chose to leave a term out. They foresaw the problem but because its occurrence cannot be observed or proved in a court, the parties *ex ante* chose not to contract about it in order to avoid the costs of opportunistic behaviour *ex post*. When faced with incomplete rules, as Schwartz explains, judges often respond by stating that it is not their role to make the law. This may appear as an exercise in formalism but in Schwartz's words, 'their response is the product of a traditional institutional constraint: courts would rather be passive than active when faced with problems they cannot solve' (1992: 274).

It is not farfetched to suggest that legislation, corporate or otherwise, will often contain provisions that condition on unobservable or unverifiable information. Plausibly, legislators are likely to be less averse to, and perhaps even not aware of, such provisions in comparison to the contractual parties whose relationship is immediately governed by the legal instrument they execute.¹² Indeed, Whincop maintained that such rules and principles 'pervade

¹² Even if foreseen by the drafters, the risk of *ex post* strategic behaviour by persons subject to the rules may be thought tolerable in the light of for example a perceived prophylactic or deterrent effect of a rule. Legislators may also seek to manage the extent of strategic behaviour by restricting the enforcement rights.

corporate law' (2001: 35) and the courts are called upon to apply them. On Whincop's assessment, the judicial response has been in line with the predictions of Schwartz's analysis: '[c]ourts have abjured rules which predicate on information which may be difficult to verify, such as the effort made by a manager, the independence of a director, or the cost of an asset sold by a director to the corporation' (2001: 35). Bratton makes a similar point when discussing fiduciary duties, *'[i]f the observation and verification of breaches costs too much, the transfer [of the noncontractual punishment function from the firm participant to the legal decision maker] accomplishes nothing. Viewed in this light, corporate fiduciary law, with its burdens of proof, collective enforcement mechanisms and substantive division between care and loyalty, amounts to a collection of solutions to the problems of observability, verifiability, and incentive to punish'* (1995: 159).¹³

As will be argued in detail below, the problem of unverifiability is a powerful explanatory force in understanding the FAC adjudication and the outcomes reported in the case data. The issue therefore is returned to repeatedly in the ensuing Chapters.

2.3.5 Information Asymmetries

The final cause of contractual incompleteness that can be identified from the law and economics scholarship concerned with adjudication of the relational contracts is central to this thesis for the reasons that will become immediately apparent. The cause occurs where one of the bargaining parties strategically withholds information that, if disclosed to the counter-party, would increase the total returns from a contract. The non-disclosure it is suggested is driven by the party's desire to increase its private gains from the bargain albeit at the expense of the parties' aggregate welfare. In these circumstances the contract is described as incomplete because the contract price does not reflect this private information. Scholars use different terms to describe this cause of incompleteness. Schwartz, for example, defines it as party preference for anonymity (1992: 279, 280). Ayres and Gertner, on the other hand, simply call it the strategic source of incompleteness (1989: 94).

The strategic kind of information asymmetry is central to this thesis because it is the apex of the modern theoretical understanding for why financial markets fail. What is more, the JSCA drafters explicitly used it to rationalise the model of corporate law they were advocating in

¹³ See also Ayres, 1992: 1404.

Russia. The connection is fairly straightforward. For simplicity, assume that the population of Russian firms that wish to raise funds from outside investors can be divided into two types – the good and the bad. The bad are under the control of the insiders who will engage in unfair self-dealing and other types of overreaching. The good are controlled by honest insiders who will not behave opportunistically. If the outside investors know the type of firm they are dealing with they will reflect it in the price they are prepared to pay in exchange for a share in the firm. In principle, no one would knowingly pay £25 for half of a £50 in a safe if the chap with the key was likely to steal it. The bad firms therefore have an incentive to be strategic and conceal their type.

Where this occurs there is a high risk of market failure also known as the adverse selection, or ‘lemons’, problem (Akerlof, 1970). If outside investors are unable to distinguish between the good and the bad firms they will discount all firms’ share prices. As a result, the honest insiders, failing to obtain the price they believe is fair for their shares, will not offer the shares to outside investors. This reduces the average quality of the firms seeking to raise funds from the investors, which in turn leads the investors to discount the share prices further. The ultimate effect is a death spiral of the market where the good firms are driven out of the financial market and share prices are forced towards zero (Black, 2001: 805). The JSCA drafters clearly thought that at the time, in mid-1990s, Russian companies were operating in the market plagued by the adverse selection problem. The law they were proposing was primarily intended to arrest that (Black, Kraakman, and Tarassova, 1998: 23-26).

Law and economics scholarship is instructive on the legislative and judicial responses to the strategic withholding of information. Of course, if one of the parties *chooses* to remain anonymous the use of the hypothetical bargaining model becomes suspect. Nonetheless, the efficiency imperative justifies intervention through judicial creativity if it can improve the pricing mechanism of the market. Two principal approaches to guide the efficiency-minded judges can be identified from the literature. The first advocates deterrence. The second, stimulating the incentives to reveal private information. Each will now be considered in turn.

Deterrence

The deterrence approach to resolving the information asymmetry appears straightforward but only, it is submitted, superficially so. There are nuances that, although well established in the law and economics literature, might have been overlooked by the corporate law scholars that

have sought to apply the approach. Helpfully, the JSCA drafters have set out what this thesis will call the orthodox approach to deterrence in the texts documenting their endeavour. They are very clear and it makes sense to quote them in full.

Having explained the adverse selection problem in the Russian equity markets, they continue, *‘[s]trong minority protections respond to this problem by reducing the risk of insider opportunism. Investors will then face a lower risk that insiders will steal most of the company’s value, and will be willing to pay more for shares. This will make higher-quality issuers interested in issuing shares, which will further raise share prices, until a new equilibrium is reached with higher share prices and a lower cost of capital’* (Black, Kraakman, and Tarassova, 1998: 25).

A parallel can reasonably be drawn with a more abstract appropriation-incentive model developed by Cooter and Freedman (1991).¹⁴ Cooter and Freedman posit that misappropriation of assets is highly profitable for agents whereas the probability of detecting and proving misappropriation by principals is small because monitoring of agents may be prohibitively costly. High profitability of misappropriation coupled with low probability of enforcement creates a deterrence deficit (1049). In such circumstances, they argue, the appropriate and perhaps usual legal response is to increase the sanction by a multiple of the agent’s benefit from self-dealing. However, since the usual fiduciary law remedies are restitutionary rather than punitive, the level of the sanction is insufficient to address the deficit (1051, 1052). Hence, as a substitute for punitive sanctions, the law should increase the probability of enforcement by for example inferring disloyalty from its appearance – presuming that agents will misappropriate the principals’ assets when it is in their self-interest to do so (1054). In a similar tone to the JSCA drafters, Cooter and Freedman’s more formal efficiency analysis explicitly favours strong protections for principals and cautions against any legal measures that would raise the costs of enforcing anti self-dealing rules such as the Part XI JSCA and that would thus reduce the probability of their enforcement.¹⁵

Expressed in this manner, the deterrence approach offers the same prescription to the courts as the investor protection principle – ‘interpret ambiguities in favour of claimants / investors’.

¹⁴ The model is a particular form of the principal-agent model the authors developed to analyse efficiency of the fiduciary duties in the context of the shareholder – director conflicts of interest but it is sufficiently general to apply to the conflicts of interest between majority and minority shareholders.

¹⁵ The authors reconcile the existence of fairness test in the US jurisprudence by highlighting that the burden of proving fairness rests with the agents (1054, 1055).

It is fair to suggest then that it might suffer from the same shortcomings. And indeed, the approach has not escaped criticism. For example, Anglo-American corporate law scholarship has pointed to the well trodden point namely the forgone value from mutually beneficial transactions that are invalidated or deterred as the costs of the deterrence approach (Easterbrook and Fischel, 1993: 441-444).¹⁶

There is, however, a more subtle criticism albeit not of the deterrence *per se* but of the orthodox approach to it. It also concerns ‘harmless’ related party transactions and it is as follows.

Thus, it is common ground that strong minority protections, especially the ones that presume disloyalty from its appearance, could lead to invalidity of, or liability for, innocent transactions that do not involve overreaching. In doing so, such rules can, and plausibly are likely to, have an adverse impact on the deterrence of harmful expropriation. This is because the rules reduce the insiders’ incentives not to expropriate outside shareholders. As Posner put it, albeit in a different context, ‘greater accuracy in the determination of guilt increases the returns to being innocent’ (1998: 1483). The point is not limited to criminal law. That greater accuracy in adjudication increases deterrence has long been recognised by the law and economics scholars as an important consideration in all areas of law concerned with deterrence (Png, 1986; Polinsky and Shavell, 1989; Posner, 1998; Kaplow, 1994).

In this regard, it is notable that in common law jurisdictions that adhere to the strong no conflicts approach such as the UK courts have equitable jurisdiction to make *quantum meruit* awards to fiduciaries¹⁷ as well as a statutory jurisdiction to grant relief to directors and officers in certain circumstances.¹⁸ Although the scope of the discretion is uncertain, its exercise concerns honesty of the defendants’ conduct (Kershaw, 2009: 408-410, 491-493), i.e. the sort of circumstance where a breach of conflict of interest rules does not involve overreaching.

¹⁶ Dammann (2007: 706) provides an interesting critique but from somewhat different perspective. He argues that related party transactions rules generally are inefficient in focusing on individual transactions, an approach which *inter alia* favours controllers that are better positioned to extract rather than create value.

¹⁷ *Boardman v. Phipps* [1967] 2 AC 46, awarding compensation ‘on a liberal scale’.

¹⁸ Section 1157 of the UK Companies Act 2006.

The existence of these measures is difficult to reconcile with what was described above as the orthodox approach to deterrence. And scholars have struggled to do so, the point clearly put by Kershaw (2009: 492):

‘This is somewhat difficult to understand as clearly any equitable allowance granted to a fiduciary in breach of his duty softens the deterrent effect of the rule: the possibility of receiving some payment through an equitable allowance increases, however marginally, the incentive a director or a trustee has to take an opportunity and breach his duty.’

Indeed, those that have sought to rationalise this discretion have done so on the basis that it assists ‘with the delivery of productive economic activity’ (Lowry and Edmunds, 2003: 197)¹⁹ or is ‘necessary to spur the fiduciary to discover and exploit opportunities’ (Easterbrook and Fischel, 1993: 442)²⁰ – in short to temper the strict approach’s frustrating effect on mutually beneficial transactions.

However, on the basis of the analysis presented above, the discretion is squarely reconcilable with deterrence: in relieving liability for honest behaviour it makes honest behaviour and the decision *not to* overreach more attractive, and hence *strengthens* deterrence of expropriation. As noted above, the law and economics scholarship has recognised this effect on deterrence since Png’s 1986 article shown that ‘to the extent that an individual who has not violated the law will be made to pay damages, the cost of violating the law, relative to not doing so, will be reduced. The result will be more violations of the law’ (101). If anything then, the discretionary jurisdiction in the UK is itself perhaps a tacit acknowledgement that the strict no conflicts approach, in punishing honest behaviour, can under-deter.²¹

¹⁹ Commenting on the section’s 1157 predecessor section 727 of the UK Companies Act 1985.

²⁰ Commenting on *Boardman v. Phipps* [1967] 2 AC 46.

²¹ The judgments delivered in *Boardman v. Phipps* are revealing. Contrast the trial judge Wilberforce J as he then was justifying the payment as compensation for skill and work done: ‘*It seems to me that this transaction, i.e., the acquisition of a controlling interest in the company, was one of a special character calling for the exercise of a particular kind of professional skill. If Boardman had not assumed the role of seeing it through, the beneficiaries would have had to employ (and would, had they been well advised, have employed) an expert to do it for them. If the trustees had come to the court asking for liberty to employ such a person, they would in all probability have been authorised to do so, and to remunerate the person in question. It seems to me that it would be inequitable now for the beneficiaries to step in and take the profit without paying for the skill and labour which has produced it.*’ ([1964] 1 WLR 993 at 1018); with Lord Cohen: ‘*I desire to repeat that the integrity of the appellants is not in doubt. They acted with complete honesty throughout ...The trial judge concluded by expressing the opinion that payment should be on a liberal scale. With that observation I respectfully agree.*’ ([1967] 2 AC 46 at 104). There is a clear difference of emphasis here, for Lord Cohen the payment is a reward for honesty. Lord Denning is clearer still: ‘*If the defendant has done*

Put short, there are limits to the deterrence solution to the adverse selection problem even on its own terms. The analysis is of direct relevance to the assessment of the FAC's procedural rule jurisprudence in the ensuing Chapters. Throughout the period surveyed in this thesis, the JSCA contained neither the relief provisions analogous to those in the UK, nor the substantive fairness review by means of which the court could uphold innocent related party transactions. Only in July 2009 section 84(1) was amended to put fairness review on a statutory footing. Paragraph four of the section now states that a court must decline to invalidate a related party transaction executed in contravention of Part XI JSCA where it is 'not proved that the completion of the transaction has lead or can lead to the incurrence of losses to the company or the shareholder that has brought the relevant action, or to the occurrence of other adverse consequences for them'.²²

Information Revelation

An alternative approach to deterrence for resolving difficulties posed by information asymmetries that is advocated by the law and economics scholars concerns incentivising the parties to reveal their private information to each other. A number of studies suggest that gap-filler rules that encourage revelation of information, referred to as the 'information-forcing' rules or the 'penalty defaults', can be optimal (Ayres and Gertner, 1989; Bebchuck and Shavell, 1991, 1999; Schwartz, 1992: 282). The rules operate by placing the better-informed parties at a disadvantage if they do not disclose a particular item of information. The rules are considered efficient because they improve pricing (Ayres and Gertner, 1989; Cheffins, 1997: 298; Deakin and Hughes, 1999: 18).

Specifically in the corporate law context, Coffee famously argued that 'the optimal default rule is ... the rule that best compels each party to reveal to the other its intended use of discretionary powers ... [because] it forces those possessing private information to disclose it

valuable work in making the profit, then the court in its discretion may allow him a recompense. It depends on the circumstances. If the agent has been guilty of any dishonesty or bad faith, or surreptitious dealing, he might not be allowed any remuneration or reward. But when, as in this case, the agents acted openly and above board, but mistakenly, then it would be only just that they should be allowed remuneration.' ([1965] Ch 992 at 1021). For Lords Cohen and Denning, the reward is not simply for 'valuable work' but for the work done 'openly and above board'.

²² The requirement to demonstrate losses in a section 84 suit made its first appearance in a quasi-legislative measure, the SAC Decree No.40 of 20 June 2007. Prior to that, the earliest judgment of the SAC Presidium to hold the same was delivered in November 2002 *Постановление Президиума ВАС РФ от 12.11.02 No.6288/00*.

to the market – and hence results in more accurate pricing’ (1989: 1623),²³ provided however that any opt-outs from the strict fiduciary duty are transaction specific. As he explained, only when an opt-out provision is limited to a specific transaction, ‘the market can judge more accurately the likely diversion of funds that has been authorized’ (1989: 1668).

Put differently, where a court is confronted with a legal provision that can be interpreted in more than one way, i.e. an incomplete or indeterminate legal provision, the efficiency-minded judge ought to apply the interpretation that would fashion incentives for the efficient disclosure, if of course such is possible. *Prima facie* gap-filler rules that could encourage greater disclosure of conflicts of interest and related party transactions would likely carry significant positives for both the efficiency and the investor protection in Russia, given the link between adverse selection and promulgation of the JSCA explained above.

There are potential objections to the above, however. First, is disclosure sufficiently desirable to justify departures from the investor protection principle? If it is, the second issue is whether the Part XI JSCA and other general disclosure obligations for related party transactions in Russia provide sufficient incentive to reveal the relevant information? If these rules already provide efficient incentives to disclose conflicts and transactions – indeed, the fiduciary duties and the transaction approval regimes are considered to be information-forcing rules (Deakin and Hughes, 1999: 19, 20) – then the need to improve the incentives is probably absent. These issues are considered next.

(a) Efficient Market Hypothesis

Regarding the first issue, it may be objected that the disclosure can be efficient, and therefore sufficiently desirable to justify departures from the investor protection principle, only if the pricing of securities by the market is efficient, in other words, if the efficient market hypothesis empirically holds, which may not necessarily be the case in relation to all stock markets, or to all securities trading on a particular stock market, and at all times (Cheffins, 1997: 55-57). In particular, it may be doubted whether the emerging financial markets possess, for example, a sufficient number of experienced and adequately resourced market professionals to perform the price-setting function effectively. Indeed, Jagric et al analysis of

²³ See also Cheffins, 1997: 298 – 301; Deakin and Hughes, 1999: 19, 20; Easterbrook and Fischel, 1993: 445; Whincop, 2001: 76 – 78.

the RTS-index between September 1995 and August 2004 suggests that the Russian equity market did not operate in the manner consistent with the efficient market hypothesis during the period (2005).²⁴ Does this mean that the inefficiency of the Russian capital market, its inability to perfectly price the disclosed information, would arrest the efficiency of an information-forcing judicially constructed gap-filler rule?

The answer is arguably 'no'. To maintain that information-forcing rules will meet the efficiency criterion only if the revealed information can be priced-in efficiently is setting a too high threshold. All that is necessary is that the revealed information has some usefulness to the investors (Bromwich, 1992: 116, 117). The key reason for this is that the efficient market hypothesis is itself based on the assumption that new information comes to the market (Jagric et al, 2005: 80). Without new information, there is nothing to price-in, however imperfectly. Since the capital market efficiency is predicated on disclosure, it is impossible to predicate the desirability of the disclosure on pre-existence of an efficient pricing mechanism. For this reason, the proponents of information-forcing rules suggest only that the new information results 'in more accurate' – not necessarily perfect – pricing. If anything, inefficiency of the Russian capital market would indicate the need for better disclosure, not *vice versa*.

Furthermore, irrespective of its impact on the price of a security, disclosure of related party transactions has other auxiliary beneficial effects because it permits shareholders to determine how to respond to the disclosed related party transaction: whether to demand that the transaction be approved at the general meeting;²⁵ whether to commence the section 84 JSCA claim; whether, and to what extent, to retain their shareholding or to 'exit' the firm (Kraakman et al, 2009: 49).

Assuming, on the basis of these reasons, that disclosure of related party transactions is generally desirable, the second issue can now be considered.

²⁴ The authors used Hurst exponent to test their hypothesis. The value of 0.5 indicates that markets follow the 'random walk'. Values in excess of 0.5 indicate that market is inefficient. During the study period RTS values varied from the highest of approximately 0.7 to the lowest of approximately 0.59.

²⁵ Section 53(1) JSCA allows 2% shareholders to add items to the general meeting agenda; section 55(1) allows 10% shareholders to request the holding of an extraordinary general meeting.

(b) Section 82 and Other Mandatory Disclosure

Russian disclosure regime for related party transactions is ineffective. This has been readily highlighted by the literature.²⁶ Section 82 is the principal measure that governs disclosure under Part XI JSCA. It requires persons identified in section 81 to disclose the juridical persons where they are insiders; and the completed or proposed transactions known to them in which they may be found to be interested persons. The section has been described as ‘obviously insufficient’ because it does not clearly identify the timing of disclosure or the procedure to be followed, while the information subject to disclosure does not cover all instances of conflict of interest (Oda, 2007: 180). Albeit, the latter concern is partially addressed by section 93(2) JSCA which requires affiliated persons to notify the company within ten days of acquiring their shares.

The two measures’ most significant shortcoming is the inadequate sanction for non-compliance. Violations of section 82 attract liability under section 84(2), and violations of section 93(2) attract liability under section 93(3), for losses caused to the company by the failure to disclose. However, even assuming that shareholders have *locus standi* under sections 84(2) and 93(3) – which is unclear (Black, Kraakman and Tarassova, 1998: 462, 488), and if not, would significantly affect the effectiveness of the provisions since the insiders are unlikely to sue themselves and their affiliates – establishing causation between the non-disclosure and the loss under both provisions is ‘extremely difficult’ (Black, Kraakman and Tarassova, 1998: 461, 488; Telukina, 2005: 562, 630). Given these shortcomings, the risk of being held liable under the provisions is highly remote. The provisions therefore fail to put the better-informed parties at a disadvantage if they do not

²⁶ For example, in recognition of the problem, Black et al, 2006b propose to incorporate into JSCA an express duty of disclosure for the insiders (39). It is highly doubtful whether the proposal would be necessary if it was thought that disclosure of related party transactions was adequate. See also Glazunov, 2000: 3. Empirical evidence however is scant. This is perhaps not surprising since non-compliance with *ad hoc* disclosure requirements is hard to observe, and therefore, measure (Kraakman et al, 2009: 50). One study measures how much of the total cash flow rights are reported by the RTS-listed firms in Russia. It finds that 45.1% of the sample firms reported 75% or more cash flow rights; 42.5% reported between 50% and 75% of cash flow rights; 11.3% reported between 25% and 50% of cash flow rights; and 1.1% reported less than 25% of cash flow rights. These results, the study concludes, suggest frequent violations of disclosure requirements in Russian firms as it is not possible to explain the numbers by the combined effect of the free float and dispersed ownership (the study assumes non-transparency where the firms report less than 75% of cash flow rights) (Chernykh, 2008).

disclose;²⁷ it is highly doubtful that the two sections can be properly described as information-forcing at all.

In addition, the two sections do not require disclosure to shareholders. Disclosure under section 82 has to be made to the supervisory board, and to the internal and external auditors. Disclosure under section 93(2) has to be made to the company. A number of, overlapping, provisions apply here. Thus article 67(1.2) of the RF Civil Code entitles shareholders to receive information concerning the firms' economic activities and to inspect their accounting records in accordance with the process specified by the constitutional documents. Article 97(2) of the Civil Code requires open joint stock companies to annually disclose to the public at large their annual reports, balance sheets, and the profit and loss accounts.

The JSCA provisions are more specific. As far as the disclosure to the public at large is concerned, section 92 largely mirrors article 97(2) of the Civil Code save that it additionally empowers the federal executive organ for the securities market to establish further disclosure requirements. As far as disclosure to shareholders is concerned, section 89, prior to its amendment in 2002, required the firms to store the following documents (listed in subsection (1)) at the location of its executive organ:

- charter (including amendments), the resolution to establish the firm, documents evidencing registration of the firm;
- documents evidencing ownership of the firm's assets that are on its balance sheet;
- internal documents of the firm, approved by its general meeting or by other governance organs of the firm;
- documents concerning the representative offices and branches of the firm;
- annual financial report;
- the share issue prospectus;
- accounting books and records;
- financial reports that are provided to the relevant authorities;
- minutes of the general meetings, the supervisory board meetings, the internal auditors meetings, and the management board meetings;
- lists of affiliated persons;

²⁷ Because conflicts of interest are often an 'unknown unknown', the disadvantage must be considerable in the sense of *vigorous* legal enforcement (Kraakman et al, 2009: 50). It is doubtful the rules meet this criterion.

- reports prepared by the internal auditors, by the external auditors, by the government and municipal financial control authorities;
- other documents required by the JSCA, by the firm's charter, by the internal documents, by the general meetings' resolutions, by the supervisory and management boards' resolutions and by other legal enactments of the Russian Federation.

In 2002 the above list was expanded to include the agreement to establish the firm; bulletins for voting at the general meetings and the powers of attorney for the participation in the general meetings; independent valuation reports; lists of persons who have the right to participate in the general meeting of shareholders and the right to receive dividends; other lists prepared by the firm to enable its shareholders to exercise their rights in accordance with the JSCA; the issuer's quarterly reports and other documents containing information whose publication, or disclosure by other means, is required according to the JSCA or other federal legislation.

Section 91(1) requires the firms to provide access for shareholders to all the documents listed in section 89(1) except for the accounting books and records and the minutes of the management board meetings. Prior to 2002 the process for granting shareholder access to the information was not specified. Section 89(2) only obliged firms to provide copies of the section 89(1) documents to the shareholders in exchange for a payment (not to exceed the costs of postage and copying). Following the 2002 amendments, section 91 obliged the firms to provide shareholders with access to section 89(1) documents at their executive organ's location within seven days from receiving a shareholder's request.²⁸ Section 52, however, establishes a more proactive disclosure process in mandating the firms to supply certain, largely overlapping with section 89, information to shareholders in advance of the annual general meetings.

Thus albeit sections 82 and 93(2) do not require the disclosure to shareholders, the additional provisions outlined above grant shareholders access to documents that would be disclosed under the two sections. This of course depends on the sections 82 and 93(2) disclosure

²⁸ A more significant amendment to the section specified that the shareholders (shareholder) who collectively held not less than 25% of a firm's voting share capital could have access to the accounting books and records and the minutes of the management board's meetings. The amended section 91(1) also provided that where Russian Federation, the subjects of the Federation (i.e. the RF regions), and the municipalities participated in firms (i.e. held golden shares) the firms were obliged to provide access to all their documents to the representatives of the said bodies.

actually being made: if a disclosure was not made to the company, the shareholders' information access rights become meaningless since there is nothing to gain access to. In other words, these provisions are only as effective – at forcing the revelation of the related party transaction information – as sections 82 and 93(2). If the sections are considered ineffective, so are the provisions granting information access to shareholders.²⁹

Finally, the Part XI JSCA process as a whole provides an incentive to disclose related party transactions. The approval by the general meeting or the board, whichever is required under section 83 for the particular transaction, should immunise the transaction from the section 84 invalidity claim. Related party transactions that are not approved will carry the risk of invalidity indefinitely thus placing the corporate insiders that fail to obtain the requisite approval at a disadvantage to those that do. *Prima facie* therefore, Part XI is an information-forcing regime.

However, the information-forcing property of the regime fails on one of the key reasons often given for why generally information-forcing rules are unlikely to yield efficient outcomes in many circumstances. The information would only be revealed if it is not too costly to do so, i.e. where the transaction costs are not prohibitive (Ayres and Gertner, 1991: 761; Cheffins, 1997: 299, 300; Easterbrook and Fischel, 1993: 445). It is generally accepted that at least in firms with a large number of shareholders the transaction costs involved in the general meeting approval are very high.³⁰ Even assuming that shareholders can cast their votes at no cost, which may not necessarily be the case if shareholders wish to make an *informed* decision (Clark, 1986: 181, 182; Goshen 2003: 416) the time constraints and the resources involved in calling the meeting will in practice outweigh the benefit of securing the approval for many transactions, unless they coincide with the annual general meeting (Kershaw, 2009: 435; Kraakman, 1999: 435).

Of course, the magnitude of the costs of seeking shareholder approval will vary with the range of transactions that require the approval, the greater the range the more often the approval will need to be sought, and the approval rules themselves. For example, the timing

²⁹ A more credible incentive to reveal information might be provided by section 30 of the Federal Law on the Securities Market 1996, and the Decrees issued by the Federal Service on Financial Markets. These require publication of affiliates lists and other facts that can materially affect the company. However, these provisions also suffer from inadequate enforcement. As Oda observes, 'the sanctions available for breaches do not seem to be sufficient' (2007: 191).

³⁰ For this reason Deakin and Hughes, 1999 thought the general meeting approval under the UK Companies Act 1985 was not a penalty default but more of a strong default, closer to an immutable rule, i.e. prohibition.

constraints can be ameliorated by permitting *ex post* shareholder ratification of transactions: general meeting need not be called every time a transaction proposed, it can be approved *ex post facto* at the annual general meeting. The next two sections consider the provisions of Part XI JSCA more closely to demonstrate that the costs of seeking shareholder approval under the JSCA are considerable.

(c) Section 81

This part focuses on section 81 JSCA, which defines the concept of conflict of interest. Even the JSCA drafters recognised that the section is very broad (Black, Kraakman and Tarassova, 1998: 447). The breadth of the definition renders a wide range of transactions subject to the Part XI approval and at the same time raises the costs of securing the approval because the definition reduces the number of shareholders that are eligible to vote.

Section 81 JSCA lists a class of persons that may potentially have a conflict of interest in a transaction and defines the circumstances for classifying a transaction as one involving a conflict of interest for the purposes of the Part XI JSCA approval requirements. Prior to the 2002 amendments to the section the list of persons who may have a conflict of interest in a transaction included:

- a member of the company's board of directors;
- a person occupying a position in other management organs of the company; and
- a shareholder(s) owning together with affiliated person(s) 20 or more percent of the company's voting shares.

The 2002 amendments replaced 'a person occupying a position in other management organs of the company' with the following persons:

- persons performing the functions of the individual executive organ including a management organisation or a manager;³¹

³¹ Individual executive organ refers to a general director. Pursuant to section 69(2) JSCA executive organs possess all the management functions of the company except those in the exclusive competence of the board of directors or the general meeting. Section 69(1) JSCA allows the companies to assign management functions to the collegial or individual executive organs or both. In the latter case a company's charter must enumerate the competencies of the collegial executive organ

- a member of the collegial executive organ; and
- persons with the right to give mandatory instructions to the company.

Pursuant to section 81 a transaction involves a conflict of interest where these persons, their spouses, parents, children, brothers, sisters and their affiliated persons:³²

- are parties, beneficiaries, intermediaries, or representatives in the transaction;
- hold (individually or jointly) 20 or more percent of a juridical person's voting shares (units) which is a party, beneficiary, intermediary or representative in the transaction;
- occupy a position in the management organs of a juridical person which is a party, beneficiary, intermediary or representative in the transaction;
- other occasions specified in a company's charter.³³

Section 81 does not address whether the existence of conflicts has to be contemporaneous with the transactions' completion. The SAC resolved the ambiguity in its Information Letter No.62 of 13 March 2001. Paragraph 14 of the Letter stated, 'by virtue of section 81 a conflict of interest in the transaction must be ascertained at the moment of its execution'.

Albeit, the section 81 list of the circumstances that could give rise to a conflict of interest is considered exhaustive, (Telukina, 2005: 555; Shitkina, 2009: 506) the circumstances invoke terms and concepts that are indeterminate and almost all embracing.

A full exploration of the concepts and their scope is beyond the scope of this thesis.³⁴ Two especially problematic terms are worth highlighting, however. The terms are 'affiliated person' and 'beneficiary'.

and the individual organ must chair the collegiate organ. Section 69(1.3) allows the general meeting, upon the initiation of the board of directors, to transfer the functions of the executive organ to a commercial organisation (management organisation) or an individual entrepreneur (manager). Analogous provisions are contained in article 103 of the Civil Code. Such management arrangements have their roots in the early post-soviet bankruptcy legislation (RF Law N 3929-1 of 19 November 1992) when they were introduced due to shortages of competent management teams and are common in Russia today (Belov, 2009: 420). For an overview of the management structure in Russian firms see Oda, 2007: 160 – 173.

³² The 2002 amendments added that the terms 'brothers' and 'sisters' cover full and half siblings, and that the terms 'parent' and 'child' cover the relationships arising by adoption.

³³ The term 'beneficiary' and the ability to specify further circumstances in the charter which would qualify a transaction as one involving a conflict of interest for the purposes of Part XI JSCA were added as a result of the 2002 amendments to the Act.

Affiliated Persons

The JSCA does not define the concept of affiliated person. Prior to January 2002, section 93(1) of the Act stated that the concept is to be defined in accordance with the antimonopoly legislation of the Russian Federation. Subsequently, the section was amended to refer to the legislation of the Russian Federation generally. However, throughout the period surveyed in this thesis, and indeed at the time of writing, the sole provision defining the concept has been, and remains, section 4 of the Federal Law On Competition and Restrictions of Monopolistic Practices on the Markets for Goods 1991 (Gabov, 2005: 94).³⁵ Presumably section 93(1) was amended to reflect the, ultimately unsuccessful, proposals in 2000 to enact an independent statute that would have defined the concept.³⁶ The concept was only introduced into the 1991 Law in May 1998 and was subsequently amended in 2002 and 2006. Until May 1998, the Part XI JSCA operated without a definition of affiliated person.³⁷ For the present purposes it is sufficient to focus on the definition as amended in 2002.

The definition has been described as ‘self-contradictory’ (Shitkina, 2008: 427); ‘practically unworkable’ (Ioncev, 2002: 120); ‘absurd and impossible of exact understanding’ (Gabov, 2005: 109).

Section 4(25) adopts an overarching definition of affiliated persons as ‘physical or juridical persons that are able to influence the activity of juridical and (or) physical persons engaged in a commercial activity’. The definition is then followed by more precise formulations in the subsequent nine subsections, which draw an important distinction between the affiliated persons of juridical persons and the affiliated persons of physical persons that are engaged in a commercial activity, that is the registered entrepreneurs. The subsections 28 and 33 of section 4, which extend the definition of affiliates to ‘persons who belong to the same group

³⁴ For a comprehensive discussion see Gabov, 2005: 71-126.

³⁵ In August 2011 the RF government announced its intention to overhaul the definition and move to the Civil Code (Kazmin, 2011).

³⁶ The proposal is available on the National Council on Corporate Governance website available at <http://www.nccg.ru/site.xp/055054048052.html>. Accessed on 20 September 2011.

³⁷ Law N 948-1 of 22 March 1991 as amended by Federal Law 06 May 1998 N 70 – Φ3. Prior to the 1998 amendment the antimonopoly legislation contained no definition of affiliated person. The term was defined in Presidential Decree No. 1186 of 07 October 1992 on Measures for the Establishment of the Financial Securities Market in the Process of the Privatisation of Governmental and Municipal Companies which applied to the activities of the investment funds in Russia. However the JSCA’s express reference to the antimonopoly legislation precluded the application of the Decree and hence Part XI of the Act operated without a definition of affiliated person until May 1998 (Gabov, 2005: 93 fn. 1).

of persons’ as the juridical or the physical person, are particularly controversial. ‘Group of persons’ is defined in section 4(13) as a group of juridical and (or) physical persons that satisfies one or several of the conditions listed in subsections 14 – 23. Finally, section 4(24) states that provisions concerning a group of persons apply to each person belonging to the group.

In an attempt to capture the notions of influence and affiliation the definition of group of persons and, therefore, affiliates refers to persons that collectively control in excess of 50 percent of a company’s share capital. The legislative intention could not have been to make the fact of share ownership alone sufficient to bring about the circumstances of affiliation, for otherwise all the shareholders in a company would become affiliated to each other. There must be some additional basis to establish the affiliation and, to be sure, section 4 refers to agreements, transactions, trusts etcetera.

But the section also uses terms such as ‘by other means’ and ‘on other basis’. Gabov called for the terms to be confined to contracts, administrative acts, corporate charters and byelaws; but concluded that that was impossible because the terms clearly indicated that the definition was not exhaustive (2005: 104, 105). The over-inclusiveness of the group of persons definition gave rise to a genuine concern that frequently situations would arise where there would be no non-conflicted persons that could approve transactions (Shitkina, 2008a: 351; Dedov, 2004: 174, 175) or that ‘neither the company, nor the counterparty [would] have any knowledge of affiliation between them’ (Telukina, 2005: 556, 559). It lead one authoritative commentator to exclaim, albeit without offering a solution, that the list of conflicted persons ‘cannot expand practically to the infinity via the term ‘affiliated persons’, and also cannot include the shareholders’ (Mogilevskii, 2004: 184).³⁸

Finally, it is worth pointing out that some uncertainty surrounded the applicability of the definition to the State and public bodies (Mogilevskii, 2004: 185; Telukina, 2005: 629). In this respect, Chernykh’s study mentioned earlier is especially telling. According to her findings, at the 25 percent voting rights threshold, that is the threshold sufficient to trigger

³⁸ The JSCA drafters’ also thought the concept covered situations that did not ‘truly involve a conflict of interest’ extending to the transactions with persons ‘who neither influence nor benefit from the company’s decisions’ (Black, Kraakman, and Tarassova, 1998: 447). In the same vein Gabov criticised subsection 6, which on its narrowest interpretation establishes affiliation between two juridical persons if one’s managing director is an employee of another. The provision, as he stressed, is ‘illogical’ – ‘if a company appoints a new MD, who, for example, is a part-time lecturer, then the logic of the provision entails that the company and the university, which do not even suspect each others existence, become members of one group and therefore affiliated persons!’ (2005: 110).

Part XI JSCA, federal and regional governments were the ultimate owners in 48.1 percent and 9.4 percent of the sample firms respectively (2008: 179, 180). In other words, a reading of the term affiliated person entailed that almost 60 percent of the RTS traded firms would be affiliated with each other for the purposes of Part XI JSCA.

The RF Government ultimately acknowledged the problems in its Concept for the Development of Corporate Legislation for the period to 2008 (Administration of the Russian Federation, 2005: 29). It proposed to overhaul the definition and to replace it with several whose breadth would be affected according to their purposes – the widest definition was proposed for the disclosure provisions, the intermediate for defining independent directors, and the narrowest for the purposes of the related party transactions regulation (30). It has also been reported that a new provision would expressly exclude state ownership from the definition (Kazmin, 2011). As noted above, at the time of writing, the proposals are yet to come to fruition. Although in July 2006, the group of persons definition was reformed and the terms ‘by other means’ and ‘on other basis’ were removed.³⁹ But crucially, these reforms did not affect status quo *ante* during the surveyed period.

Beneficiaries

As outlined above, section 81 brings a transaction within the scope of Part XI JSCA whenever insiders, their relatives, or affiliates are, *inter alia*, themselves beneficiaries under the transaction; or they own in excess of 20 percent shareholding or hold managerial posts in the juridical persons that are beneficiaries under the transaction. The term beneficiary was only introduced into section 81 in January 2002, as part of the general reforms to the JSCA that were enacted in August 2001. Throughout the period surveyed in this thesis the term remained undefined under the JSCA. The SAC provided the definition, for the purposes of the section, only in June 2007 in its Decree No. 40.

The provision was introduced to tackle avoidance of Part XI JSCA by structuring transactions through, what Davis once called (1985: 45), ‘straw men’ – *prima facie* independent third parties. The deficiency in the original section’s 81 focus on the transactions that were executed directly with the insiders and their affiliates was highlighted by the JSCA drafters; but was not addressed by the legislature until 2002 (Black, Kraakman, and Tarassova, 1998:

³⁹ Section 9 of the Federal Law No. 135-FZ on Protection of Competition 2006.

447, 448). To reduce the risk of avoidance, the drafters proposed that the Part should also apply where the insiders or their affiliates ‘acquire directly or indirectly, as a result of such transaction, property, property rights, or other rights having monetary value’ (1998: I-88). Albeit the proposal did not use the term beneficiary its purpose and substance were the same. Thus, on the one hand, the term was necessary for the Part XI to operate effectively in protecting the minority shareholders.

On the other hand, however, the term expressly brought transactions involving third parties within the scope of the Part, the third parties whose independence may only be *prima facie*, but may also be genuine. Indeed, the fact that the remit of Part XI JSCA began spreading to unconnected third parties spurred the SAC into action, albeit only in 2007. A discussion note accompanying the SAC’s initial proposal for the Decree No.40 expressly discussed the effects on the third parties.⁴⁰ It cited the Decision of the Presidium of the SAC that shortly preceded the proposals as giving rise to the Court’s concerns.⁴¹ The case involved a shareholder challenging the validity of a mortgage over the defendant’s property granted in favour of a third party bank to secure the credit facility provided to the defendant’s parent.⁴² The note cited it as an example of the ‘widespread use [of the term beneficiary] in bad faith by debtors (and connected with them mortgagors and guarantors) in order to escape the repayment of debt or to make the creditor’s position particularly difficult’.

To be clear, this is not a critique of the overly broad definitions of conflicts of interest. As Black et al point out, ‘the concept of conflict of interest is difficult to define’. And their survey of a number of jurisdictions showed that courts generally resist providing precise definitions of conflicts (Black et al, 2006b: English version: 66). Rather, the intention is to highlight that the breadth of section 81 JSCA brings a large measure of transactions within the requirements of Part XI and, more importantly, renders the approval all the more expensive to secure as it disqualifies more shareholders’ eligibility to vote.

⁴⁰ See materials of the SAC Presidium meeting of 8 February 2007. Available at <http://www.arbitr.ru/vas/presidium/prac/23099.html>. Accessed on 1 February 2014.

⁴¹ In fact the original explanatory note presented at an earlier SAC Presidium meeting had the case number in its title. See materials of the SAC Presidium meeting of 14 December 2006. Available at <http://www.arbitr.ru/vas/presidium/prac/23088.html>. Accessed on 1 February 2014.

⁴² Постановление Президиума ВАС РФ от 05.12.2006 No.9675/06.

(d) Section 83

Section 83 sets out the Part XI JSCA approval process for related party transactions. It has been already noted above that the near prohibitive direct costs of holding a general meeting especially in firms with a large number of shareholders for most related party transactions appears to be generally accepted. While not to say that the rules on calling general meetings and on quorum are seamless or not costly, they are unlikely to be of such magnitude so as to impede the holding of a general meeting in and of themselves.

However, in addition to the direct costs of general meetings, there are indirect costs, which are augmented by one important provision of section 83. Because of the indirect costs a further number of transactions, that would otherwise be of a sufficient value to make the expense of the general meeting worthwhile, would conceivably not be put before the shareholders, which means a further erosion of the information revelation potential of the Part XI JSCA process.

The indirect costs arise because related party transactions often take place in the bilaterally monopolistic context (Posner, 1998: 69) – the controllers and minority shareholders can only trade with each other (Whincop, 2001: 19, 80).⁴³ In such contexts, the parties' asymmetric information concerning each others' valuation of the asset subject to the transaction creates strong incentives for strategic behaviour: the parties are likely to misrepresent their private valuations in order to capture the larger share of the gains from trade.⁴⁴ In other words, the controllers may offer too little to secure the minority's consent, or the minority may ask for too much, with the consequence that transactions that would leave all the parties better off are not approved.

Furthermore, certain shareholders may have incentives to vote against the transaction even if it benefits shareholders as a group. The common examples are conflicted voting whereby a transaction may benefit the company and shareholders as a group but may leave an individual shareholder worse off (Kraakman et al, 2009: 167); and holding out, refusing consent hoping that the forgone gains from the transaction would force the company to buy shareholder's approval with a side payment (Easterbrook and Fischel, 1991: 101).

⁴³ Yablon, 1991 stating that bilateral monopoly almost invariably features in fiduciary cases (505).

⁴⁴ Ayres and Talley, 1994: 1030; Kaplow and Shavell, 1996: 733, 734; Goshen, 2003: 402; Calabresi and Melamed, 1972: 1106; Shavell, 2004: 90, 91.

To be sure these problems are not exclusive to Russia. Every jurisdiction that requires shareholders, or their representatives, to approve transactions creates a risk of strategic voting. However, the problem is likely less pressing in jurisdictions with diffuse corporate ownership structure such as the UK and the US. In these jurisdictions the majority, as opposing to unanimity, approval requirement coupled with the shareholders' collective action problem make such strategic behaviour difficult to coordinate. The costs of coordinating among the diffuse constituents are likely to temper the benefits of holding-out (Whincop, 2001: 82; Goshen, 2003: 417; Brudney, 1997: 616).

In contrast, in the concentrated ownership jurisdictions such as Russia, large outside shareholders can have significant holdup power even under the 'majority of non-conflicted minority' approval such as the one required under section 83. The JSCA drafters expressly singled out the holdup problem as a one of the principal drawbacks of their self-enforcing model (Black, Kraakman, and Tarassova, 1998: 39), acknowledging that the problem is likely to be exacerbated, not mitigated, by the collective action problem of small outside shareholders. The rational apathy of small shareholders augments the larger shareholders' ability to hold out by making it harder for the controllers to obtain sufficient votes to secure the necessary approval, as the drafters put it, 'the two concerns interact: the rational apathy of small outside shareholders increases the holdup power of larger shareholders' (1998: 39).

Nevertheless, the drafters proposed that the majority of non-conflicted minority approval under Part XI JSCA require the majority of *all*, rather than present and voting, non-conflicting shareholders meaning that the votes of all the rationally apathetic, that is non-participating in the general meeting, shareholders are treated as if they would be cast against the transaction (Black, Kraakman, and Tarassova, 1998: 457, 458).⁴⁵ As the result a greater majority of non-conflicted shareholders will be necessary to approve the transaction increasing both the direct costs of obtaining the approval and the hold out power of a greater number of smaller block holders. It is therefore fair to assume that a greater number of transactions would not take place or would proceed without the approval at the risk of invalidity in Russia.

⁴⁵ Prior to the 2002 reforms the JSCA did not expressly state whether the consent of all non-conflicted shareholders was required. Section 83(3) only stated that the approval of majority of non-conflicted shareholders was required without stipulating how the majority is to be determined. However, the 2002 revisions put the matter beyond doubt. Section 83(4) now expressly states that the majority of all non-conflicted shareholders is necessary to pass the resolution under the section.

Second, there are good reasons to believe that the indirect costs of obtaining the approval are likely to be lower in legal systems where insiders can defend transactions on the ground that they were substantively fair. If shareholders are more likely to approve transactions then greater number of transactions would be submitted for the approval thus improving the information-forcing effect of Part XI JSCA. The arguments concern the transactions that are frustrated by the strategic, holding out, behaviour due to the parties' information asymmetries – i.e. the transactions that are not precluded by the direct costs of summoning the general meeting.

The principal argument⁴⁶ rests on Johnston's original insight that uncertainty in *ex post* judicial outcomes could improve *ex ante* bargaining efficiency in circumstances where asymmetric information impedes negotiations (Johnston, 1995). Where an ownership entitlement is contingent on *ex post* judicial imprimatur under some imprecise balancing test, such as the substantive or entire fairness, a party to the negotiations, a controlling shareholder for example, can credibly threaten to take the entitlement if the counterparty, a minority shareholder for example, holds out for a higher price. In such circumstances, Johnston explains, the ownership of the entitlement itself 'becomes a matter of incomplete information *ex ante*' (258), the uncertainty that makes the credible threats possible and hold out behaviour difficult.

To the extent that the strict no conflicts approach *ex ante* assigns entitlements to minority shareholders more definitively, it precludes controllers' ability to threaten the taking credibly to mitigate holding out. This reduction in the minority shareholders' ability to hold out pursuant to the fairness review entails that greater number of transactions – that generate sufficient value to surmount the costs of holding a general meeting – would be approved and, therefore, submitted for the approval thus improving information revelation to the shareholders.

⁴⁶ Another reason for maintaining that the fairness review, in jurisdictions where it is available, is likely to result in greater number of approved transactions concerns the higher litigation costs the approach imposes on the parties – the parties would have to submit evidence on value in addition to demonstrating whether or not the Part XI approval requirements were infringed – and the controllers' ability to complete transactions without disinterested shareholders' consent. This follows from the Ayres and Talley's demonstration that the autarkic disadvantage of litigation costs causes liability rules to have an efficiency advantage over property rules when the direct transaction costs of bargaining are surmountable (Ayres and Talley, 1995: 242-248). As the authors explain liability rules can lead to an increase in efficiency-enhancing transactions due to both parties' 'wishes to avoid losing litigation costs from nonconsensual takings. Because the threat of litigation costs increases the marginal costs of bargaining breakdown, the defendant will not attempt to extract as much from the plaintiff, and the plaintiff will be more willing to accept the defendant's offer' (248).

Even more instructive is the Ayres and Talley's extension of Johnston's analysis, which shows how liability rules, such as the fairness review, can improve bargaining in the bilaterally monopolistic contexts by reducing both parties' room to lie about their reservation values.⁴⁷ The basic premise of their bargaining model is that where an ownership to an entitlement is uncertain, that is probabilistic, the parties do not know whether they would ultimately end up as a buyer or a seller in the transaction. This 'identity crisis' reduces their incentive to misrepresent the value of the asset subject to bargaining – as potential sellers they have the incentive to overstate the value; as potential buyers they have the incentive to understate the value – thus reducing the bargaining range and making the agreement more likely.

The model is applicable in the context of obtaining the approval for a related party transaction. This stems from the fact that, in a fairness review jurisdiction, the controllers and the minority are not just bargaining over the asset. Rather they are also, implicitly, bargaining over each other's options to force a non-consensual transaction and to rescind it (Ayres, 2005: 13-38). Consider an example where a controlling shareholder wishes to purchase an asset belonging to the company. Here the controller is a buyer of the minority ownership interest in the asset and of the minority's option to rescind the sale if the controller siphons off the asset without the minority's approval. As such, his incentive is to understate the value of the asset. At the same, he is a seller of his option to take the asset without the minority's consent. As such, his incentive is to overstate the value of the asset, since the higher the asset's value, the greater the threat of harm to the minority shareholders and hence the more valuable is the controller's option.

The minority, on the other hand, are in the reverse position. They are the sellers of their ownership interest in the asset and of their option to rescind. As such, they have the incentive to overstate the asset's value. At the same time, they are the buyers of the controller's option to take the asset non-consensually and hence have the incentive to understate the value of the asset. The parties' incentives as buyers and sellers pull in the opposite direction thus reducing the bargaining range over the asset. This effect is considerably more difficult to achieve under the strict no conflicts approach because the controller's option to take the asset

⁴⁷ Ayres and Talley, 1994: 1072-1082, 'the identity crisis – uncertainty about whether a bargainer will ultimately become a buyer or a seller – reduces both parties' *incentives* to lie' (1077 emphasis in original). See also Ayres, 2005: 142-183.

is near worthless. The controller is only buying, and the minority are only selling – there is no Ayres and Talley’s identity crisis.⁴⁸

There is little new in this analysis. It implicitly features in Goshen’s economic assessment of the Delaware rule, which, instead of immunising, reverses the burden of proof of demonstrating a transaction’s fairness onto claimants where the transaction with the controlling shareholder has been approved by the disinterested minority. The analysis leads Goshen to conclude that ‘shifting the burden of proof provides the market with the incentive to seek the support of the majority of the minority, thereby reducing the need for judicial judgment on the value of the deal’ (2003: 429). To arrive at this conclusion Goshen relies on the arguments advanced above, albeit, contrary to his conclusion, his actual assessment fails to explain the reverse burden. Rather, his assessment supports full immunity for the approved transactions under the fairness review.⁴⁹

Thus, essentially Goshen argues that the possibility that a controlling shareholder could complete a transaction without the approval reduces the minority’s ability to hold out: their negotiating power ‘is limited by the knowledge that even if their support is not given, the controlling person can still make the deal and bear the burden of proof that it is fair’ (429). At the same time, the controller would have to offer a higher price than it would have been if the minorities’ support had not been sought. Shifting the burden of proof, Goshen explains, provides the minority with ‘some negotiating power: the minority has ‘something’ to sell to the majority’ (429). In effect, Goshen concludes, this is an insurance transaction – ‘the controlling person pays a premium (increased price) to the minority in order to increase the chances that the deal will not be stalled by litigation or struck down by the courts’ (429).

All this seems consistent with the above analysis save that the reverse burden of proof has little to do with it; or, to be precise, it does, but in manner contrary to what Goshen suggests. In fact, the reverse burden diminishes the minority’s negotiating power in contrast to the situation where the approval attains full immunity for the transaction: the minority has ‘something’ to sell to the majority, but the ‘something’ is less than that would otherwise transpire under the full immunity regime. On this assessment, the reverse burden makes the

⁴⁸ Whincop, 2001 considered and rejected this possibility in the context of the Anglo-American fiduciary duties because it gives the insiders greater ability to holdout (82). Yet, this overlooks the fact that the insiders are not just selling their option to take, they are also buying the asset. The effect is in both directions not just one.

⁴⁹ This is not to say that shifting the burden onto the claimants does not incentivise seeking the approval, it possibly does, but for reasons other than those relied on by Goshen.

approval more likely but, contrary to Goshen, by diminishing, not enhancing, the minorities' negotiating power. In other words, the effect of the Delaware's reverse burden is to reduce the transactions' bid – ask spread thus making the approval more likely.

The Delaware's reverse burden for the approved transactions involving the controlling shareholders – as opposing to those involving directors and officers where, a more differential to the interested party, business judgment rule governs (Goshen, 2003: 427) – acknowledges the minorities' hold out power in such transactions. Indeed, Whincop has expressly noted the positive implications of Johnston's and Ayres and Talley's analyses for allowing courts to examine transactions on their merits but his focus on the transactions involving the directors has lead him to disregard this advantage because, in these circumstances, he thought the risks of strategic bargaining and hold out were small given the costs of the collective action problem under the majority rule for widely dispersed shareholders (Whincop, 2001: 80, 82). In Russia, in contrast, as suggested above, the strategic bargaining and holdup problems are considerable. To the extent a fairness review (with or without the reverse burden) arrests these problems, it leads to a greater number of approved transactions than would ensue under the strict no conflicts approach, and, therefore, to more information revealed to the shareholders. But, as already noted above, a fairness review was not explicitly introduced in Russia until the Decree No.40 in 2007 and was not put into the statute until July 2009.

In conclusion, it is worth pointing out that even if Part XI approval forces some revelation of information to outside investors it does not immediately rule out the efficiency of other measures that could induce disclosure. Thus, Bebchuck and Shavell demonstrate that all that is necessary is for a gap-filler norm to induce the disclosure at a lower cost (Bebchuck and Shavell, 1991: 286, 291, 292, 301 – 303). However, given the deficiencies in the Russian disclosure provisions and the high direct and indirect costs of Part XI JSCA approval set out in the preceding paragraphs it is reasonable to think that the information-forcing gap filler rules could lead to a considerably greater flow of information concerning conflicts and transactions to the shareholders. As a minimum, the above discussion suggests that there is scope for greater information revelation.

This topic is returned to in the discussion of the statute of limitations and contemporaneous ownership rule in Chapter 5, which deals with the procedural rules in shareholder cases.

Hypothesis

The analysis and arguments presented above now permit the formulation of the judicial bias hypothesis as follows.

With respect to the case data judgments delivered against the claimants the judicial bias hypothesis will not be substantiated if those judgments accord:

- (a) with a higher order legislation or legal precedent;
- (b) the investor protection principle; or
- (c) the aggregate welfare maximisation.

Put differently, if none of the (a) – (c) criteria can reasonably explain a particular FAC decision then the decision will support the hypothesis that the judges are biased or incompetent.

Finally, the ensuing Chapters reformulate the hypothesis to reflect the doctrinal and economic analysis applicable to the specific rules under consideration in those Chapters. However, the fundamental tenets set out in (a) – (c) remain the same throughout.

CHAPTER 3

PROCEDURAL RULES IN COMPANY ACTIONS

Introduction

It is a truism in company law that rules designed to regulate conflicts of interest must have some prospect of being enforced to realise their function. For Davies, for example, the proposition that the UK fiduciary obligations require as a minimum a credible threat of enforcement is a banality (2008: 605). At the same time, litigation may not be desirable in every case where the rules are infringed. For this reason, the role of the law, as Davies explains, is to determine the person or persons ‘who can safely be entrusted’ with deciding whether in a particular case the litigation should be instituted (605, 606). The same is likely to be the case in Russia. It is reasonable to suggest that Part XI JSCA may also require measures to control undesirable litigation at least to the extent that would not detract from the credibility of the threat of the Part being enforced. The legal measures that determine who can be entrusted to bring actions under Part XI JSCA, which for convenience will be referred to as procedural rules, form the subject of this and the following Chapters.

This Chapter is concerned with the procedural rules in the Part XI JSCA lawsuits brought by companies. The only procedural rule that features in the case data, and that has inhibited the ability of companies to enforce Part XI JSCA, is the statute of limitations. The Chapter, therefore, examines the relevant Russian legislation and appraises its application by the FAC against the normative criteria developed in Chapter 2 namely, the judicial bias hypothesis. To recall, the hypothesis holds where the FAC completes incomplete law with gap filler rules that deviate from the investor protection principle unless the rules maximise the aggregate welfare of the shareholders. Put differently, the hypothesis will not be supported by the FAC jurisprudence that either (i) follows the legislation or a higher order legal precedent (loosely defined to include the SAC’s Decrees, Information Letters, jurisprudence and the jurisprudence of the RF Constitutional Court); or (ii) instantiates the investor protection

principle meaning the most claimant friendly rule interpretation is adhered to; or (iii) is Kaldor-Hicks efficient.

The structure of the Chapter is as follows. Section 3.1 examines the merits and demerits of companies enforcing Part XI JSCA with a particular focus on identifying the circumstances where company actions may pose a credible avenue to redress the minority shareholder expropriation at the instance of the controlling inside shareholders. The legal analysis begins in section 3.2 with the discussion of the legislation, precedent and literature pertinent to the statute. The discussion of the law is followed by the efficiency analysis in section 3.3, which seeks to ascertain what interpretations of the statute, in so far as the law and precedent leave scope for interpretation, would maximise the parties' joint welfare. Finally, the judicial bias hypothesis concerning the statute is formulated and the FAC cases are appraised against it in sections 3.4 and 3.5 respectively.

3.1 Problems with company enforcement of Part XI JSCA

This Chapter began with an observation that for corporate law scholars the need for a realistic prospect of enforcement of related party transactions rules is a truism to the point of banality. Perhaps another truism in corporate law is that companies are unlikely to furnish such a prospect. Reasons for this contention are set out in section 3.1.1 below. However, because weaknesses in redressing expropriation of the minority shareholders are in themselves insufficient reasons to curtail company lawsuits under Part XI JSCA the subsequent section 3.1.2 also deals with positive arguments in favour of subjecting companies' litigation to a procedural rule filter.

3.1.1 Suboptimal enforcement problems

Ordinarily the right to commence legal proceedings vested in a company is exercised by its senior management by virtue of their general management powers and this is also true for Russian companies incorporated under the JSCA. Under article 103 of the RF Civil Code 1994 and sections 65 and 69 JSCA the supervisory board is endowed with all the competences to decide issues of general leadership of a company save for those in the exclusive competence of the general meeting. The executive organ of the company, whether individual or collegiate, is endowed with all the competences to effectuate leadership of the

company's ordinary activity safe for those in the exclusive competence of the general meeting or the supervisory board. The decision to institute legal proceedings, whether under Part XI JSCA or otherwise, is not allocated to the exclusive competence of either the general meeting or the supervisory board meaning that, in principle, either the board or the executive organ could commence proceedings under Part XI JSCA depending on whether litigation is considered a matter of general leadership or of the company's ordinary activity.¹

However, this uncertainty in the allocation of powers between the board and the executive organ is of little practical significance in the context of enforcing Part XI JSCA. The majority, if not the whole, composition of both the board and executive organ will be constituted by the controlling shareholders or their appointees. And it can reasonably be expected, that neither organ would be likely to institute proceedings disadvantageous to the interests of the same controlling shareholders. Indeed, the JSCA drafters were very much alive to this possibility in observing that 'the company has the right [to bring proceedings under Part XI JSCA], but is unlikely to' (Black, Kraakman and Tarassova, 1998: 462). It is fair to suggest then, as others have done albeit outside Russia (Parkinson, 1993: 217; Reisberg, 2007: 1), that for a realistic prospect of enforcement Part XI JSCA, as with the regulation of related party transactions elsewhere in the world, there has to be an agent independent from the controlling shareholders and their appointee management who is able to bring actions under the Part.

This is not to say that companies are unlikely to ever bring proceedings under the Part to redress harm to the minority shareholders. The case data points to the contrary. Over the eight-year period surveyed in this thesis companies brought approximately half of the cases before the FAC. In certain, limited, circumstances companies may not be under the control of the expropriators and some of the company cases are likely to fall into this category.

Thus, the first circumstance involves expropriation by a 'rogue director'. It is conceivable that the controlling shareholders' appointees may engage in self-dealing. If they do, they will expropriate the controllers and the minority alike. When the wrongdoing is discovered the director will likely be dismissed and the proceedings to invalidate the offending transactions instituted. The curb on the managerial agency costs, of which the rogue director self-dealing is an example, is perhaps the most often cited advantage for acquiring a minority position in

¹ On the unclear demarcation of competences between the supervisory board and the executive organ in Russian law see Black, Kraakman and Tarassova, 1998: 369-371.

the companies with controlling shareholders (Levmore, 1982: 76; Gilson and Gordon, 2003: 785). Such shareholders have the incentives and the means (and often little alternative)² to monitor the management, which also benefits the minority shareholders. In fact, because of the controlling shareholder monitoring it is likely that few cases involving the rogue director expropriation would be brought under Part XI JSCA. As has been authoritatively stated with respect to companies where ownership is concentrated, which is the case in Russia, ‘managerial self-dealing is not an issue, because controlling shareholders can curb it effectively’ (Kraakman et al, 2009: 178).

The second circumstance is where the control over a company has passed from the expropriators into the hands of others. In principle, there is nothing to stop new controllers from causing the company to sue to undo the damage done by their predecessors. Here too, however, there is likely to be a small chance of the company bringing the action (Marsh 1966: 55; Hoel, 1975: 186), for two reasons. First, the courts may be unsympathetic to such actions. In companies with concentrated ownership structure control sales are likely to be consensual transactions (Kraakman et al, 2009: 256), meaning that the acquirers are expected to conduct pre-acquisition due diligence of the company’s balance sheet not least to price the transaction (Sepe, 2010: 6). The price would reflect the company’s assets and liabilities on the date of the transfer. Subsequent recovery of the assets would constitute a windfall and there is evidence from outside Russia of judicial reticence to allow companies to proceed in such circumstances (Marsh 1966: 55). The reluctance to allow such action is perhaps understandable for they involve expenditures on redistributing wealth from vendors to the acquirers, which is an inefficient deployment of scarce resources (Cohen, 1991: 973-975; Cooter and Ulen, 2004: 8, 112; Farnsworth, 2007: Ch.7).

Of course, actions brought by the new controllers may not have purely redistributive effect. They may deter the incumbents from self-dealing. But they may also, and perhaps more likely to, deter the incumbents from selling the control, which is undesirable (Enriques, 2004: 785). It is a basic principle of economics that resources should, and tend to if voluntary exchange is possible; gravitate to their most valuable uses (Posner, 1998a: 11; Shavell, 2004: 18; Farnsworth, 2007: 20). There is always a risk that acquirers may value control more than the incumbents by being more adept at expropriating than generating value (Bebchuck, 1994;

² Exit is unlikely to be an option even in the presence of deep and liquid markets as market participants would perceive the controller as bailing out on the basis of private information thus leading to a collapse in the share price (Coffee, 1991: 1329).

Coffee, 1984). However, on the one hand, the available empirical evidence indicates that transfers of control generate value in the aggregate (Alexandridis et al, 2010: 1671). On the other hand, lawsuits by the new controllers are unlikely to provide an effective channel against inefficient sales of control. Such lawsuits would dissuade the inefficient shifts in control only in limited situations where the new controllers themselves anticipate subsequently selling the acquired controlling interest. Moreover, there are arguably better means to reduce the occurrence of the inefficient control sales (Sepe, 2010).

The second reason to believe that actions brought by the companies subsequent to a change of control are likely to be infrequent applies irrespective of the judicial attitude and is arguably more important. As noted above, the incumbent controllers are likely to determine whether control shifts occur and, presumably, also to whom and on what terms. The incumbents may simply not sell to the acquirers they suspect likely to challenge pre-existing related party transactions. Alternatively, and expectedly, they could seek to protect the pre-existing transactions through undertakings not to sue, or other contractual arrangements of a similar kind, with the acquirers. Therefore, company actions at the instance of the new controllers are unlikely to feature prominently in the Part XI JSCA litigation landscape, which renders their merits or demerits largely academic.

Finally, expropriators may lose control to an insolvency practitioner, an administrator or liquidator, if the company becomes financially distressed. Insolvency practitioners, acting pursuant to their management powers bestowed upon them by the insolvency legislation, would then be able to issue proceedings under Part XI to retrieve assets wrongly transferred to the controllers. Plausibly, as far as the enforcement by companies is concerned, actions instituted by the insolvency practitioners may provide the most credible threat of the Part XI proceedings being instituted against the controlling shareholders. Indeed, the case data supports this proposition. Some 37 cases were brought before the FAC by the companies under the control of liquidators and administrators representing 44 percent of the total actions brought by companies during the surveyed period. It is also worth mentioning here that enforcement by insolvency practitioners has also been recognised as a potentially viable deterrent against expropriation in the literature dealing with jurisdictions other than Russia (Parkinson, 1993: 237, 238; Armour et al, 2009: 714, 715).

However, outside the financial distress situations, it is reasonable to conclude that companies are unlikely to offer a realistic prospect of enforcement under Part XI JSCA to remedy the

controlling shareholder overreaching. Perhaps for this reason the discussion of company actions is sparse in the general company law scholarship. Rather, the central focus of the discussion is the identification of the persons independent of controlling shareholders and management – the persons who by definition solvent companies cannot be – that can be entrusted with enforcing related party transaction rules.³

With respect to the merits of curtailing companies' litigation, the company law scholarship is also noticeably silent. This is perhaps unsurprising. The principal concern is with companies not bringing actions when they ought to, not vice versa. There are 'fewer concerns', as Kershaw explains, 'in relation to a board decision to commence such litigation' (2009: 537). And such concerns as are there, are in themselves extensions of the principal concern – the worry that companies may pursue litigation only half-heartedly due to the same conflicts of interest that prevent them from pursuing litigation at all (Kershaw, 2009: 537). In Russia, in contrast, company lawsuits gave rise to specific and related concerns during the eight-year period surveyed in this thesis. These concerns are considered next.

3.1.2 Improper enforcement problems

Two concerns with companies' litigation under Part XI JSCA can be identified from the literature and also from the case data. The concerns are opportunism and protection of third parties.

As to the former, it has eluded definition beyond the very general but has nonetheless gained broad acceptance among the law and economics scholars (Williamson, 1985: 47-49; Posner, 1998b: 101 – 104).⁴ The particular behaviour relevant to this Chapter falls within the narrowest of definitions of opportunism. Mankind has known it at least since Machiavelli's time (Machiavelli, 1531/2: 57) and Hobbes thought the State should deter it (1651: Pt. I. Ch. 14: 18-20). One of the earliest accounts of the judicial experiences with Part XI JSCA has also identified it as a feature in the Part's enforcement landscape (Novoselov and Mametov, 2000: 83). Machiavelli's description is perhaps the plainest, '... a prudent ruler cannot, and must not, honour his word when it places him at a disadvantage and when the reasons for

³ Davies, 2009: Ch. 17; Kershaw, 2009: Ch. 15; Parkinson, 1993: Ch. 8; Clark, 1986: Ch. 15.

⁴ Probably the most famous and general definition belongs to Williamson – 'self-interest seeking with guile' (1985: 47). For a critique of opportunism literature for lack of definition see Cohen, 1991: 953-957.

which he made his promise no longer exist... And no prince ever lacked good excuses to colour his bad faith' (Machiavelli, 1531/2: 57). In the December 2000 SAC Vestnik (a leading legal periodical in Russia and the official publication of the SAC) two FAC judges wrote of cases brought under section 84(1) JSCA in remarkably similar terms. Judges Novoselov and Mametov criticized the unfettered rescission right under Part XI JSCA in part for sanctioning litigation by the 'so called conflicted persons with the blatant intention to repudiate agreements' (83). The behaviour therefore appears to be as familiar in the modern-day Russia as it was in the renaissance Europe.

Economics literature defines such behaviour as *ex post* attempts to redistribute risks and returns already allocated by agreement between the parties (Goetz and Scott, 1981: 1139). Opportunism of this kind is inefficient because it does not increase the value of the agreement and therefore produces no social benefit. On the contrary, parties' investments in the opportunistic behaviour and measures to prevent it are 'deadweight losses' that deplete social wealth (Cohen, 1991: 973, 974; Goetz and Scott, 1981: 1139; Farnsworth, 2007: 67). Thus, it was suggested above that some company claims brought at the instance of the new controllers might fall into this category of opportunism.

It is likely that the constituency of opportunistic company litigation under Part XI JSCA is broader. The case data is indicative on this point. The insolvency cases account for 44 percent of the companies' litigation only. This then begs the question namely, what explains the remaining 56 percent of the cases, or at least a considerable part thereof, given that the companies are unlikely to challenge transactions that benefit controlling shareholders and the new controller and rogue director litigation is unlikely to be conspicuous for the reasons explained above?

Opportunism must be the answer. It is the only remaining option. Lawsuits are brought to rescind transactions for reasons that have little or nothing to do with remedying insider overreaching. Rather they are brought upon occurrence of events *ex post facto* the transactions that render the original agreements disadvantageous to the controlling shareholders.

Prevention of opportunistic litigation therefore provides a positive argument in favour of curtailing companies Part XI actions at least in the situations outside insolvency. However, it does so only partially. On the one hand, it may not always be obvious whether a lawsuit is opportunistic making it a difficult task to devise a procedural rule that would act as a filtering

mechanism. Such a rule might preclude claims against rogue directors for example, the claims that may well be inconspicuous but nonetheless possible. On the other hand, the possibility of rescission at the instance of the company even in claims tainted with opportunistic motives may discourage unapproved related party transactions and incentivise the insiders to seek the board or general meeting approval under Part XI JSCA. Arguably, for the controlling shareholders the possibility to recoup their losses in a Part XI action is an incentive not to seek recourse to the Part's approval processes. However, they may find themselves under pressure to obtain the approval nonetheless. The pressure is likely to come from a constituency that stands to lose from the opportunistic lawsuits namely, the third parties that transact with the companies.

For every unapproved transaction where companies succeed in asserting their entitlements to assets, third parties are likely to suffer reliance losses (Armour and Whincop, 2007: 445). The possibility of the losses in turn creates an incentive for the third parties to take precaution – to engage in ameliorative behaviour to reduce the incidence of companies shifting their losses onto their counterparties via the section 84(1) restitution remedy. For example, the third parties may employ greater efforts to screen transactions for conflicts of interests; insist on the Part XI approval, or on undertakings that the approval will be obtained, or simply decline to enter into a transaction where there is a risk of it being held to have involved related parties. To be sure all these efforts are costly. However, it is well established in the economic theory that investments in precautionary measures will be cost justified until the cost of a little more precaution (marginal cost) equals the resulting reduction in the expected losses (marginal benefit), that is when the efficient level of precaution is achieved (Cooter and Ulen, 2004: 320-325; Cooter, 1985; Farnsworth, 2007: Ch.5)

There is an important caveat to this analysis. It explains why third parties' interests require, and are almost universally accorded, some form of legal protection. The caveat is as follows. In cases where two parties can take precaution, the efficiency requires both of them to take it (Cooter and Ulen, 2004: 325, 326). This efficiency condition is called double responsibility at the margin (Cooter, 1985: 4). The condition cannot be achieved if companies are allowed to rescind unapproved related party transactions in every instance. Because all the losses from the transactions can be externalised onto the third parties there is little incentive for the companies to take precautionary measures. Arguably, if the companies were prevented from obtaining restitution in every case, the controlling shareholders would have greater incentives to monitor their management; the new controllers would have greater incentives to conduct

the pre-acquisition due diligence; and the minority shareholders and creditors would have greater incentives to monitor the controlling shareholders in the vicinity of insolvency. At the same time, if a procedural rule were to preclude all company actions under Part XI then the incentive for the third parties to take precaution would be reduced. Put short, a blanket rule that places losses on companies or on third parties in every action cannot achieve double responsibility at the margin.⁵

Ordinarily legal doctrines such as the apparent authority or good faith purchaser for value without notice that allow third parties to avoid restitution in certain circumstances achieve (or strive to) double responsibility at the margin (Farnsworth, 2007: 55). The doctrines incentivise both third parties and companies to take precaution: third parties, to meet the legal standard to avoid restitution (for example, to be more scrupulous with transactions where the price is suspiciously low); companies, to avoid the residual risk of losses on transactions if a third party is found to have met the standard (Cooter and Ulen, 2004: 330; Cooter, 1985: 7).

Of course, whether they in fact achieve the efficiency condition depends on the legal standard being set at the efficient level (Cooter and Ulen, 2004: 330). And while it is well accepted in the law and economics literature that the efficient standard should allocate the losses to the party that could have avoided them at the least cost (Farnsworth, 2007: Ch. 7), in practice identifying ‘least cost avoiders’ may be a fact intensive exercise that is difficult to conduct *ex ante*.⁶

A court, however, may be in a better position to perform this task *ex post*, having the benefit of the full facts when a dispute is brought before it (Armour and Whincop, 2007: 446). For example, it is likely that the third party’s monitoring and precaution costs would be considerably greater in relation to low-value ordinary business transactions than in relation to large and irregular transactions (Armour and Whincop, 2007). The court should be able to determine what kind of transaction is in dispute before it and allocate the loss accordingly – to the company, by denying the restitution, if the transaction is ordinary; and to the third party, by granting the relief, if the transaction is irregular.

⁵ Nor is it possible to apportion losses between the parties in section 84(1) actions – the court must rescind or uphold the transaction, to allocate the whole loss to the company or the third party. Apportioning losses is in any case inefficient because it allows both parties to externalise some of the loss. Cooter and Ulen, 2004: 326; Cooter, 1985: 4.

⁶ Farnsworth, 2007: 55; Levmore, 1987, explaining the differences in the treatment of good faith purchasers across jurisdictions in terms of the difficulty in working out whether they are the least cost avoiders. See also Fox, 1998 arguing that in the UK the standard is set at an efficient level.

Thus, the protection of third parties provides the second reason to impose a restriction on companies' litigation under Part XI JSCA. Notably, the rationale is not restricted to lawsuits brought by solvent companies alone. The efficiency requires that transactions be upheld in cases where third parties are not the cheapest cost avoiders and this principle applies irrespective of the companies' solvency.

There is, however, an objection to the foregoing. The need to protect the interests of third parties only calls for the rules that fulfil that purpose, namely the doctrines on apparent authority and constructive notice referred to above. It might be argued that the rationale does not justify resort to procedural rules, i.e. rules that would bar certain claimants from recourse to the judicial process irrespective of the merits of their claims or, to use the above example, irrespective of whether the transaction is ordinary or irregular.

There is an answer to this objection and it is twofold. On the one hand, before 2009 the JSCA accorded no protection to third parties in the section 84 rescission claims. This being so despite the JSCA drafters' recommendation that the Part XI requirements be treated as part of the company's internal governance rather than as affecting the validity of the transactions with third parties. Specifically they thought that the rescission should only automatically apply when transactions were concluded with 'conflicted' persons directly; their close relatives; and with juridical persons that were 100 per cent owned by the conflicted persons. In all other cases the drafters proposed that the remedy should only be available if the counterparty 'knew or should have known of the violation of the conflict-of-interest rules' (Black, Kraakman and Tarassova, 1998: 461). In their 2006 report Black et al restated the recommendation proposing to amend the JSCA to specify that the section 84 remedy of invalidation of the transaction should apply 'only if invalidation will not cause harm to third parties' (2006b: English version: 5). These recommendations, however, were not adopted until June 2007, when the SAC incorporated the analogous provision in paragraph 2.3 of its Decree No. 40; and were only expressly introduced into section 84 in July 2009. These third party protections did not exist throughout the period surveyed in this thesis.⁷

On the other hand, the efficiency calls for a legal norm – rule or standard – that would offer third party interests a degree of protection while achieving the double responsibility at the margin. In principle such a norm could take any form, including one of a procedural rule, as

⁷ The SAC Decree No. 9 of 14 May 1998 contained third party knowledge provision but only regarding *ultra vires* suits under article 174 of the Civil Code. Section 84 suits proceed under article 168 of the Code.

long as it achieves the same objectives. In other words, a rule that is functionally equivalent to the more conventional doctrines that protect third parties' interests could suffice.

A procedural rule of this kind would no doubt be difficult to devise. In preventing certain types of claimants from suing the rule would operate *ex ante* and would leave the courts no room to examine the facts *ex post* to identify the least cost avoiders. To meet the efficiency condition of the dual responsibility at the margin the rule would have to perform this task for the courts *ex ante* which, as suggested above, may be impossible. Nonetheless, it will be argued below that the procedural rule adopted by the FAC in the companies' litigation performs precisely this task. Put differently, in the companies' litigation under Part XI JSCA it may be possible to identify least cost avoiders *ex ante*.

3.2 Law

Under the RF Civil Code 1994 civil actions can be barred by the lapse of time upon an application of a party to the dispute.⁸ Whether a particular claim will be time barred depends on the applicable limitations statute and there are several such statutes in Russia (Oda, 2007: 101-103). Thus, article 196 of the Code sets the general limitation period at three years, which pursuant to article 200(1) is triggered on the date a person discovered or should have discovered the infringement of her rights. The general limitations period is complemented with special limitations statutes. The special statutes must be applied in accordance with the rules for determining the general limitation period contained in articles 195, 198 – 207.⁹ This Chapter is concerned with one such special statute, to be found in article 181 of the Code, which is the statute applicable to the lawsuits to invalidate transactions including those brought under the JSCA.

The applicability of the article 181 special limitation period to the section 84 rescission suits is unambiguous. It is manifest in the article's title: '*limitation periods for invalid transactions*'. The actual limitation period for such suits, however, is ambiguous because article 181 contains two limitation periods, which differ in both the duration and the commencement date. Thus, until July 2005, the article 181(1) limitation period was 10 years.

⁸ The relevant provision, article 199 of the Code, does not permit courts to dismiss claims on this ground on their own motion.

⁹ Article 197 (1). Unless the legislation contains an express provision to the contrary (article 197(2)).

In July 2005, it was reduced to three.¹⁰ Under the article, in its original and amended versions, the period commences from the day performance of the transaction began. The article 181(2) period, on the other hand, is, and has always been since the Code was enacted, one year. The period commences from the date when ‘*the claimant discovered or should have discovered the circumstances that provide the grounds for invalidating the transaction*’.¹¹ Plainly, article 181(1) limitation period cannot account for the time barred claims surveyed in this thesis, at least not for those decided prior to the July 2005 amendment. Until July 2005, the 10-year period would have covered all related party transactions completed since the JSCA came into effect in January 1996. Article 181(2) must have been and, as shown below, was the basis for the dismissals on the ground of lapse of time.

Of course, and despite observations to the contrary in the literature,¹² it is how the courts construe article 181(2), rather than the one-year period *per se*, that is critical to a claimant’s ability to enforce Part XI JSCA. Ten years is a longer period than one year and the shorter article 181(2) period could potentially diminish the claimant’s position. However, this would be the case only if the article 181(2) period is construed to commence on the same date as the article 181(1) period, namely from the performance of the transaction, which does not follow from the plain reading of article 181(2). The one-year period is triggered when the claimant ‘discovered or should have discovered’ that she has a cause of action, the date that, at least in principle, could occur several years since the date of performance. Indeed, there may be situations where the ten-year period would lapse while the one-year period would not. This means that judicial preference for article 181(2) over article 181(1) *prima facie* need not necessarily lead to inferences of bias. And for this reason the greater part of the ensuing discussion is concerned with the article’s 181(2) trigger date and the questions of notice and knowledge attribution.

At the same time, the FAC’s application of article 181(2) has clearly inhibited a considerable number of actions brought under Part XI JSCA that would not have been time barred under

¹⁰ RF Federal Law No. 109 – FZ of 21.07.2005.

¹¹ This is subject to one exception, namely transactions that are invalid pursuant to article 179. The article 179 transactions are the transactions effected under duress, violence, threat etc. The commencement day for such transactions is the day when the duress, violence, threat etc have ceased. This is expressly stated in article 181(2).

¹² See Vereshchagin, 2007 observing that the article 181(1) period for void transactions is ‘much longer’ than the article 181(2) period for voidable transactions and hence the voidable characterisation ‘seriously deteriorates’ a claimant’s position from the limitations statute perspective (224).

article 181(1). Furthermore, the court has construed article 181(2) trigger date analogously to article 181(1) – from the completion of the transaction. To what extent this construction of article 181(2), which for convenience will be referred to as the contract-based standard for attributing claimants with knowledge of their causes of action, supports or does not support the judicial bias hypothesis cannot be posed solely as a question of the knowledge attribution. It is the court's resort to article 181(2) in the first place that enabled it to deploy the contract-based standard in relation to a one-year limitation period. The resort to article 181(2) also requires examination to test the hypothesis. Thus, the next section considers to what extent legislation and legal precedent predetermined the judicial preference for article 181(2) over article 181(1).

3.2.1 Transaction characterisation

The applicability of one or the other article 181 period depends on whether the impugned transaction is characterised as void or as voidable. Void transactions are subject to the article 181(1) period. Voidable transactions are subject to article 181(2). On 31 October 2000 the SAC held that transactions completed in violation of Part XI JSCA were voidable.¹³ Therefore, for the purpose of appraising the FAC's cases, the SAC precedent settled the law regarding which limitations statute governed related party transactions in favour of article 181(2) in late 2000.

Prior to the emergence of the SAC jurisprudence there was uncertainty over the question of how related party transactions should be characterised under the Civil Code and hence over the applicable limitations statute. Thus, the classification of invalid transactions into void and voidable is to be found in articles 166 to 179 of the Civil Code.¹⁴ And neither the articles nor the JSCA expressly state whether transactions contravening Part XI JSCA are void or voidable. Although one of the Code's provisions does provide a fairly straightforward basis to characterise the transactions, its wording and juxtaposition with section 84(1) JSCA gave rise to an ambiguity. The provision is article 168, which governs the classification of transactions whose invalidity arises from non-compliance with the law or other legal edicts. Since Part XI JSCA arguably falls within the meaning of 'the law or other legal edicts', the

¹³ *Постановление Президиума ВАС РФ от 31.10.00 No.3020/00.*

¹⁴ For the full description of all the different invalid transactions under the articles see Oda, 2007: 86 – 101.

applicability of article 168 to the related party transactions is not controversial. The ambiguity arose, and remained unresolved until the SAC's 31 October 2000 decision, because transactions within the ambit of article 168 could either be void or voidable depending on the encroached legislation and, as already noted, the JSCA did not specify explicitly the nature of the Part XI transactions.

Thus, article 168 provides that a transaction that does not comply with the law or other legal edicts is '*void, unless the law provides that such transaction is voidable, or does not provide other consequences of the infringement*'. The appropriate characterisation under the article therefore depends on the legislation, which an impugned transaction allegedly violates: if the legislation is silent on the issue then the transaction is void; if the legislation specifies that the violating transactions are voidable, then the transaction is voidable.

Unfortunately, prior to amendments to JSCA in August 2001, section 84(1) was neither silent nor positively specified that related party transactions were voidable. The section stated that '*a transaction, in the completion of which there is a conflict of interest, completed with an infringement of the requirements specified in section 83 of the instant Federal Law, may be held invalid*'. The significance of this wording, and the ambiguity it gave rise to, become apparent once placed in the context of articles 166 - 179 of the Civil Code, which define and identify void and voidable transactions. In particular, two factors indicating the voidable characterisation can be surmised from these provisions and only one of these was present in section 84(1) thus giving rise to the ambiguity over how related party transactions ought to have been characterised.

On the one hand, section 84(1) contained terminology used in the Civil Code to identify voidable transactions. Notably, the Civil Code does not explicitly describe voidable transactions as 'voidable' (*osporima*); only void transactions are expressly labelled 'void' (*nichtozhna*) in the Code.¹⁵ Instead, articles that do not contain the term 'void', namely articles 173 – 179, refer to invalid transactions subject to these articles as transactions that '*may be held invalid by a court*'. This wording reflects the article 166(1) stipulation that the invalidity of voidable transactions depends on judicial imprimatur.¹⁶ Hence, the use of the words 'may be held invalid' in section 84(1) suggested that transactions violating Part XI JSCA requirements were voidable.

¹⁵ See articles 169 – 172 of the Civil Code.

¹⁶ Void transactions, in contrast, are invalid *ab initio* (without the recognition to that effect by a court) according to article 166(1).

On the other hand, certain provisions associated with voidable transactions, namely an explicit designation of persons who have standing to challenge the transactions, were missing from section 84(1). The necessity for the explicit designation follows from article 166(2.1), which states that only the persons specified in the Civil Code may bring actions to challenge the validity of voidable transactions. Thus, one would expect to see the relevant provision expressly designating the persons with the standing to challenge voidable transactions because, otherwise, in the light of article 166(2.1), the provision would be unenforceable. Indeed, articles 173 – 179 all expressly designate the persons who have standing to challenge the voidable transactions specified in these articles. For void transactions such designation is unnecessary because pursuant to article 166(2.2) ‘*any interested person*’ can petition a court to rescind void transactions.¹⁷ Thus, articles 169 – 172, which classify transactions within their scope as void, are silent on the question of who has standing under the articles. Therefore, section’s 84(1) silence concerning the *locus standi* was more consistent with the void characterisation of related party transactions.

The outcome of the section’s 84(1) original drafting, read in conjunction with article 168, was two interpretations concerning the proper characterisation of related party transactions that violated Part XI JSCA. A court could construe such a related party transaction as voidable by holding that section 84, in stating that the transaction ‘may be held invalid’, was the law that ‘provide[d] that such transaction [was] voidable’. Alternatively, a court could construe the related party transaction as void by holding that section 84, in not designating persons who have standing under the section, did not ‘provide[] that such transaction [was] voidable’. In sum, from the perspective of the legislative construction, a court could characterise the transactions as void or voidable depending on how much weight it attributed to the absence of an express *locus standi* in section 84(1).

In its judgment of 31 October 2000, the SAC recited that under article 168 transactions were void unless the contravened legislation stipulated that the transactions were voidable. The court held that section’s 84(1) use of the words ‘may be held invalid’ entailed that the related party transactions completed in breach of Part XI JSCA were voidable. Interestingly the court did not consider whether the lack of an express standing under the section indicated the contrary (or the potential implications of its decision for the interpretation of article

¹⁷ Albeit the term ‘any interested person’ is narrower than in the colloquial use it is sufficiently wide to include a wide range of claimants affected by the void transaction. The term covers any person who could obtain a pecuniary benefit from a court’s judgment. Shestakova, 2008: 103.

166(2.1)). However, two judges of the FAC did consider the issue in their article in the December 2000 issue of the *SAC Vestnik*, which argued that the appropriate characterisation of the Part XI transactions was voidable. Thus, Judges Novoselov and Mametov, thought that the absence of the *locus standi* was a legislative oversight rather than an intentional categorisation of the transactions as void (2000: 85). They suggested that the oversight could be resolved, absent an express legislative amendment, by interpreting section 84(1) by analogy with section 45(5) of the Federal Law on the Limited Liability Companies 1998 (LLCA), which stated that the transactions involving a conflict of interest ‘*may be held invalid upon a claim by the company or a member*’ (87). The legislative intervention followed in August 2001 when the words ‘*upon a claim by the company or a shareholder*’ were inserted into section 84(1), which ‘made it clear that [a transaction with an interested party effected in violation of Part XI JSCA] is a voidable transaction’ (Oda, 2007: 181).

Thus, at the time of writing, the academic commentary is unanimous in positing that transactions completed in violation of Part XI JSCA are voidable. Opinions, however, diverge in respect to the point of time when the characterisation issue was settled as a matter of law. For Oda, for example, as is apparent from the above quote from his treatise on Russian Commercial Law, there was uncertainty concerning the proper characterisation of related party transactions and it was addressed by the August 2001 amendments to section 84(1) JSCA (2007, 180). In contrast, others posit that related party transactions were always voidable (Vereschagin, 2007: 223; Gabov, 2005: 360; Shapkina, 2002: 178) or that they were always voidable but some courts occasionally characterised the transactions as void (Telukina, 2005: 576-577).

It is of course possible that the legal analysis above overplays the relevance of *locus standi* to the construction of article 168 and section 84. May be the SAC was restating the law rather than settling hereunto unsettled legislative uncertainty. Indeed, for these commentators the August 2001 JSCA reforms were inconsequential to the characterisation question since the relevant wording ‘may be held invalid’ remained unaltered (Telukina, 2005: 576-577).

From what point in time then did the legislation and precedent sanction the FAC’s recourse to article 181(2) limitation period rather than to the period in article 181(1)? An answer is necessary to formulate a hypothesis against which to test the FAC’s jurisprudence. It is helpful therefore to set it out clearly before proceeding to the next section.

It is difficult to agree with the view that the voidable nature of related party transactions was clear from the point of enactment of the JSCA. As will become evident below, the case data does not support it. Furthermore, the SAC decision was shortly followed by the Novoselov and Mametov article,¹⁸ referred to above, which was published in the *SAC Vestnik*. The article put forward the case for characterising related party transactions as voidable, which would have been an arguably meaningless exercise were it always plain that voidable was the correct characterisation.

As to the relevance of the August 2001 JSCA amendments, it is reasonable to suggest from the FAC's perspective, and for the purpose of appraising its jurisprudence, a higher order legal precedent was already established by the time the August 2001 JSCA amendments were enacted and came into effect.

Finally, it is worth mentioning that on 10 April 2003 the RF Constitutional Court delivered the ultimate source of certainty in this area of Russian law by holding that shareholders had *locus standi* in Part XI litigation and that therefore section 84(1) in its pre-2001 reform form was not unconstitutional in characterising transactions as voidable.¹⁹ This position, however, has already been secured by the 2001 revision of section 84.

In summary, from the late 2000 the SAC established legal authority for treating related party transactions completed in contravention of Part XI JSCA as voidable. From that point in time the FAC's resort to article 181(2), a consequence of the voidable characterisation, would have been sanctioned by the SAC and would not support the judicial bias hypothesis for the purposes of this thesis. Prior to that point, it is plausible to suggest that the FAC had a measure of discretion in its construction of related party transactions as void or voidable, and hence over the applicable article 181 limitation period, given the ambiguity created by the article 168 of the Code and section 84 JSCA.

How should the FAC have characterised the transactions in the absence of an unambiguous answer in the legislation? What is the appropriate characterisation of the related party transactions under the Civil Code within the parameters of the judicial bias hypothesis? The answer to this question, and whether a clear answer is indeed possible, must await the

¹⁸ In fact, the decision was only published in the January 2001 *Vestnik*, i.e. in an issue subsequent to the publication of Novoselov and Mametov's article.

¹⁹ *Постановление Конституционного Суда Российской Федерации от 10.04.2003 по делу о проверке конституционности пункта 1 статьи 84 Федерального закона Об акционерных обществах в связи с жалобой открытого акционерного общества Приаргунское.*

efficiency analysis in section 3.3.1 below. Before turning to that discussion, the next section discusses the legislation and judicial precedent pertinent to interpretation of article 181(2). The objective is to draw out ambiguities and certainties in the law to ascertain to what extent the legal framework provides a sufficient yardstick against which to test the FAC jurisprudence.

3.2.2 Knowledge attribution under article 181(2)

The drafting of article 181(2), when ‘the claimant discovered or should have discovered’ the relevant circumstances that gave rise to her cause of action, provides for the actual and a constructive standard for attributing the knowledge to claimants. Albeit the article does not explicitly specify which standard should prevail in a particular case; its plain interpretation suggests that the standard that provides the earliest trigger point, which in most situations would be some form of constructive knowledge, should prevail. Thus, if it is established that the claimant became aware of her cause of action over a year prior to bringing proceedings and the article 199(2) petition is made, the statute requires the court to dismiss the action. If the court allowed the claimant to proceed because she should have made the discovery at a later date, within the one-year period, then the claimant’s actual knowledge would become irrelevant. If this is what the legislature intended, then article 181(2) could simply state that the statute is triggered on the date when a claimant should have discovered the cause of action.²⁰

For this reason claimants that learn of their cause of action over a year prior to bringing proceedings are more likely to deny this fact than admit it and insist on being allowed to proceed because the statute would not have expired under some form of constructive knowledge standard. Since claimants either do not have the requisite actual knowledge, or, those that do, deny having it, it is foreseeable that the majority of article 199(2) applications would require the courts to apply a constructive knowledge standard. At this stage, however, it is sufficient to note that the RF Civil Code explicitly legislates for departures from the actual knowledge standard – in this regard the law is ‘complete’ – and therefore, the

²⁰ The converse is also true. If the court determines that the claimants should have found the cause of action over a year prior to bringing the claim, but allows them to proceed because they actually found out at a later date, within the limitation period, then the constructive knowledge standard would become irrelevant. If this was intended, then statute could simply state that the period is triggered from the date the claimant found out of the cause of action.

jurisprudence deviating from the standard should not necessarily be taken as evidence in support of the judicial bias hypothesis. In this respect the legislation offers a sufficient refutation of the hypothesis.

However, if the drafting of article 181(2) is complete in explicitly allowing deviations from the actual knowledge standard, it is ‘incomplete’ in specifying a permissible scope of such deviations. A more elaborate definition of the term ‘when the claimant ... should have discovered’ is absent from the RF Civil Code. It is therefore impossible to determine which constructive knowledge standard would or would not support the judicial bias hypothesis solely in terms of its adherence to the article 181(2) text.

In April 2003, in its judgment mentioned above, the RF Constitutional Court developed the term further. The Court held that the start of the limitation period must commence from the moment *‘when the legally entitled person discovered or had a real opportunity to discover not only the fact that the transaction took place, but also that it was executed by persons interested in its conclusion’*.²¹ Yet, the Court did not elaborate what the ‘real opportunity to discover’ entails. Neither the SAC, nor commentators have sought to do so.

So formulated, the standard lacks any objective criteria on the basis of which knowledge may be attributed to claimants. It is conceivable that claimants, defendants and the judges will have different views on whether a claimant had a ‘real opportunity to discover’ the existence of her cause of action. Indeed, it is questionable whether the words add any additional substance to the Code’s test of ‘should have discovered’. This lack of objective criteria makes it impossible to use the Court’s standard as a yardstick against which the FAC’s jurisprudence can be appraised, i.e. to formulate a falsifiable hypothesis.

One objective criterion has been suggested in the literature, however. A number of authors who have considered the issue have thought that in introducing the phrase ‘real opportunity’ the judgment directs the courts not to infer a claimant’s knowledge too readily – not to use some ‘lower’ standard of knowledge attribution. Albeit the judgment does not identify what such ‘lower’ standard might be, the authors have criticised the courts’ use of constructive knowledge to trigger the limitation period from the date of the transactions’ completion, i.e. the courts’ use of the contract-based standard.²² The standard, it has been observed, is at

²¹ *Постановление Конституционного Суда Российской Федерации от 10.04.2003*, para. 5.2.

²² Black et al, 2006b: English version: 53; Telukina, 2005: 578; Gabov, 2005: 372; Shitkina, 2008: 522; Dobrovolskii, 2006: 224, 225.

odds with the legal precedent set by the Constitutional Court's judgment (Black et al, 2006b: English version: 53). Importantly for the present purpose, the contract-based standard contains a sufficient degree of objectivity to formulate a falsifiable hypothesis at least in relation to the cases heard *ex post facto* the Constitutional Court's judgment. In principle it should be straightforward to identify the FAC's decisions invoking the contract-based standard and to then treat them as evidence in support of the judicial bias hypothesis.

This approach, it is submitted, is specious. First, even if judicial recourse to the contract-based standard to dismiss cases is reproachable the standard still fails to provide a meaningful measure against which to appraise the FAC's jurisprudence. This is because such a yardstick would only catch judgments of the lowest denominator, in effect presuming that any decision on the statute of limitations ground involving a claim brought over a year after the disputed transaction's completion is inconsistent with judicial bias hypothesis. Arguably, a meaningful measure should be based on the standard that the courts should use. A yardstick of this kind would be capable of identifying all the cases that fall short of the standard as supporting the judicial bias hypothesis. And it is here that the literature falls short. In denouncing the contract-based constructive knowledge standard as incompatible with the Constitutional Court's judgment, it fails to explain what the 'real opportunity to discover' test entails. It argues what the standard cannot be, without explaining what it is, or what it should be. The literature, as is the case with the legislation and superior legal authorities, is silent on a definition of the constructive knowledge standard that is underpinned by objective and measurable criteria. To this extent it offers little assistance in formulating the judicial bias hypothesis.

Second, the literature is too quick to criticise the contract-based standard and in particular to rule out its application in relation to *every* kind of claimant.²³ While the economic merits of the contract-based standard are explored in section 3.3.2 below and in Chapter 5, it is worth mentioning here that the common sense suggests that whether a claimant had the 'real opportunity' to discover the relevant facts at some earlier date so as to preclude the section 84 claim will depend on the characteristics specific to a particular claimant. It is conceivable,

²³ The exception is Dobrovolskii, 2006 who identifies that the statute of limitation jurisprudence differs in company claims from that in shareholder claims (222). However, he does not consider efficiency rationale of the one-year period, confining his conclusions to observing that in these cases the company prevented from suing because of limitation period expiry can find a cooperating shareholder to file the claim (225, 229). This is an important point and is returned to below. Dobrovolskii, however, does not draw a distinction between different types of shareholders (229 - 233) as this thesis does.

for example, that majority shareholders, board members and minority shareholders may all have different access to the corporate books and records and would therefore differ in their ability to discover the facts pertinent to expropriation. This suggests that *prima facie* all types of claimants cannot be treated on the basis of the same constructive knowledge standard, and in particular, as will be argued below, the contract-based standard is efficiency enhancing in relation to certain types of claimants.

For the purpose of the legal analysis with which the immediate section is concerned, it is worth pointing out that the Constitutional Court judgment did not consider whether variations in the constructive knowledge standard are permissible under article 181(2). Importantly, it did not rule them out. In the passage quoted above the Court refers to claimants as the ‘legally entitled persons’, which commentators have interpreted as companies and (presumably all types of) shareholders,²⁴ implying that the Court was setting a ‘one-size-fits-all’ standard. The interpretation, however, is only convincing when read in isolation from the remainder of the Court’s judgment. A more holistic reading casts doubt over its validity. The constructive knowledge standard set by the Court was arguably directed at the minority outside shareholders only: the case was brought before the court by a minority shareholder, *OAO Priargunskoe*; and throughout the judgment the Court expressly refers to the ‘minority shareholders’²⁵ – ‘the weakest side in the system of corporate relations’²⁶ who are ‘incapable during the stage of a transactions conclusion ... to protect their legitimate interests’.²⁷

In holding that the imposition of the article 181(2) one-year limitation period is not of itself unconstitutional, the Court was concerned with balancing the minority shareholder protection with the need to check the minority shareholder opportunism. For example, in the concluding paragraph the Court observes that its ruling does not obstruct the federal legislature from ‘perfecting the mechanism for protecting shareholders’ rights, without infringing the stability of relations in the sphere of economic exchange, to secure in particular the rights of the minority shareholders, while excluding the possibility for them to abuse their rights’.²⁸ In stressing that the claimants must have a real opportunity to discover the relevant facts, the Court was concerned that otherwise the limitation period may prove an

²⁴ See Black et al, 2006b: English version: 53. Curiously Russian version of the report does not do so.

²⁵ The term in Russian is ‘миноритарные акционеры’. In the judgment’s 6 paragraphs the term appears in the following subparagraphs 2.4, 3.4, 4.2, 4.7, 4.8, 6.1.

²⁶ para. 3.4.

²⁷ para. 4.7.

²⁸ para. 6.1.

insurmountable obstacle to the section 84 claims for the minority outside shareholders, that it would effectively *de facto* bar their ability to enforce Part XI JSCA, and would therefore fail to balance the protection from expropriation with the need to curb opportunism.²⁹

On this basis, the judgment does not preclude the development of a different standard to the claimants who represent ‘a stronger side in the system of corporate relations’ – for whom the contract-based standard would not *de facto* deny their *locus standi*. At no point does the Court rule out a stricter standard for such claimants. As a question of legal interpretation therefore, a varied constructive knowledge standard is possible under article 181(2). In this respect the law is ‘incomplete’: the Court has not prohibited the use of contract-based standard in all circumstances.

To conclude the legal analysis, the legislation and precedent do not offer an adequate objective yardstick against which to evaluate the judicial application of the statute of limitations for judicial bias. The next section pursues this task.

3.3 Analysis

The preceding discussion described ambiguities in the Russian statute of limitations applicable to the related party transactions governed by Part XI JSCA. Such ambiguities existed at different points in time in relation to (i) what statute was applicable to such transactions and (ii) the interpretation of the specific, article 181(2), limitation period. It is fair to suggest that the ambiguities provided the FAC with a measure of discretion in interpreting the relevant provisions of the Civil Code. This section seeks to establish how the court should have interpreted the provisions using efficiency as a normative guide in order to formulate a falsifiable hypothesis to appraise the case data against.

The section is comprised of two principal parts. Section 3.3.1 offers a commentary on the difficulties of conducting the economic analysis in relation to the transaction characterisation question. Section 3.3.2 principally focuses on knowledge attribution under article 181(2). It explores what standards of knowledge attribution lead to joint welfare maximisation in claims brought by companies. In particular whether the efficient construction of article 181(2) differs for company claimants depending on whether or not they are subject to the

²⁹ Indeed the claim was that the application of statute of limitation was effectively denying *locus standi* to minority shareholders under section 84, and for this reason, the Court’s decision states that section 84 grants *locus standi* to minority shareholders.

control of insolvency practitioners. Thus, it examines whether for the financially distressed companies the standard that triggers the start of the limitation period from the date of appointment of the insolvency practitioner might be efficient. For convenience the thesis will call it the appointment-based standard of knowledge attribution. For other companies it will be argued that the contract-based standard is the efficient norm. Finally, section 3.3.2 also discusses the circumstances pursuant to which the contract-based standard might be the welfare maximising knowledge attribution norm in the financially distressed companies also.

3.3.1 Transaction characterisation

How should have the FAC characterised related party transactions in the absence of an unambiguous answer in the legislation? What is the appropriate characterisation of the transactions under the Civil Code within the parameters of the judicial bias hypothesis? For a number of reasons it is difficult, and perhaps impossible, to answer the question in the abstract.

The first difficulty arises because there is a number of practical outcomes of characterising related party transactions as void or voidable each of which potentially affects the investor protection and the efficiency differently. The applicable statute of limitations, the principal concern of this Chapter, is but one such outcome. Another is the *locus standi*, that was alluded to above. Under article 166(2.2) ‘any interested person’ can petition a court to apply the consequences of invalidity for void transactions. The term is sufficiently broad to include the companies, their shareholders, creditors and perhaps even the state (Shestakova, 2008: 102 – 115; Vereschagin, 2007: 224). In contrast, for voidable transactions article 166(2.1) requires an express designation of the persons with the standing to sue. Since, until its amendment in August 2001, section 84(1) was silent on the *locus standi*, the voidable characterisation could, in effect, result in the non-enforcement of Part XI JSCA during the period prior to the coming into effect of the August amendments in January 2002. Albeit, as will become apparent from the FAC judgments discussed below, the court has not doubted the companies’ *locus standi* to enforce Part XI JSCA, there was a real issue concerning the persons other than the companies who could bring claims under the Part (Vereschagin, 2007: 224; Gabov, 2005: 363).

Another difference in outcomes concerns courts' discretion to invalidate void and voidable transactions. As noted above, article 166(1) states that void transactions are invalid *ab initio*. *Prima facie* the invalidity of a void transaction is not for the courts. In contrast, under the article, voidable transactions have to be held invalid by a court. However, the difference in terms of whether a court's involvement is necessary is somewhat artificial – a court application is necessary also for void transaction in order to obtain relief. The article 166(1) distinction therefore would be somewhat meaningless if the declaration to invalidate a voidable transaction was mandatory for the courts. It follows that article 166(1) perhaps implies that the courts have a measure of discretion in invalidating voidable transactions. Indeed, it was already pointed out above that articles 173 – 179, and section 84(1) JSCA, all state that the impugned transactions 'may' be held invalid suggesting that the declaration is discretionary in nature. Thus, Shapkina, for example, has argued, that the existence of the discretion is apparent from the law's formulation of a voidable transaction: 'such a transaction *may* be held invalid by a court, which means, it may not be so held and [can therefore] retain its legal force' (2009: 160).

To answer the question – how should the FAC have characterised the related party transactions – would therefore necessitate an analysis of all the three outcomes' impact on the investor protection and/or of their costs and benefits to ascertain the overall effect of the outcomes on the parties' joint welfare.

This difficulty is further augmented because the outcomes of characterising transactions as voidable are potential. These outcomes may or may not transpire in the actuality depending on the judicial interpretation. This means that, on the one hand, there may be no consequential differences in terms of the investor protection or joint welfare from characterising transactions as void or as voidable. On the other hand, the range of potential outcomes that would require evaluation would increase considerably. For example, voidable characterisation may lead to the courts finding that shareholders do not have standing to enforce Part XI JSCA. Yet, this need not be the case as Judges Novoselov and Mametov suggested in their *Vestnik* article cited above. Courts could permit shareholder *locus standi* by, for instance, interpreting section 84(1) JSCA by analogy with section 45(5) LLCA. Similarly, whether the judicial discretion weakens the protection of investors or results in welfare losses also depends on *whether* the courts exercise the discretion and the *scope* of the discretion, if exercised. This potentially expands the number of outcomes of characterising transactions as void or voidable *ad infinitum* since, for example, Shapkina thought that the

courts had to evaluate ‘all the circumstances that influenced and accompanied the completion of the transaction’ to determine whether to hold it invalid (2009: 160). Even if, on a more realistic assessment, such circumstances could be confined to a finite number,³⁰ the task is still scarcely made more manageable.

Finally, the investor protection and efficiency outcomes of the characterisation are likely to vary according to the type of claimant seeking to bring the section 84(1) suit. This is most apparent in the context of the *locus standi*. It was suggested above that those in control of a company were unlikely to cause it to sue to rescind transactions that benefited the controllers. It is reasonable to suggest therefore that the effects of restricting companies’ ability to enforce Part XI JSCA would differ from restricting the enforcement by shareholders. The same holds true, as argued in detail below and the subsequent two Chapters, with respect to the exercise of the judicial discretion in invalidating the transactions and to the application of the statute of limitations.

In summary, the characterisation of related party transactions as void or voidable affects too many actual and potential variables to discern *a priori*, within the confines of a doctorate thesis, the characterisation, or the characterisations in combination with specific outcomes, that would provide the greatest degree of protection for the minority shareholders or that would lead to the greatest net gains to the parties’ joint welfare.

Does this mean that the thesis’s project of appraising the FAC adjudication fails at the first hurdle for the inability to formulate a normative yardstick against which to conduct the appraisal? It is submitted that the project is not futile. First, since the SAC’s judgment held that the related party transactions are voidable in October 2000, the question of how the FAC should have characterised the transactions is only relevant to the FAC cases decided during the first two years of the period surveyed in this thesis. For the cases decided in the remaining six-year period (2001 – 2006) the voidable characterisation was established as a matter of law from the perspective of the FAC.

³⁰ For example, in July 2009 section 84(1) was amended placing some of the more pertinent circumstances on the statutory and mandatory basis. Section 84(1) now states that courts shall decline to invalidate a transaction executed in contravention of Part XI JSCA where (i) the votes of a claimant shareholder could not have influenced the outcome of the vote on the transaction; or (ii) it is not proved that the completion of the transaction caused or could cause losses to the company or the shareholder; or (iii) the transaction received an *ex post facto* Part XI JSCA approval; or (iv) that the counter-party to the transaction did not know and should not have known that the transaction was executed in contravention of Part XI JSCA.

Second, and importantly, it is possible to evaluate outcomes individually; to examine the adjudication to ascertain whether the court pursued a specific outcome in characterising a transaction as void or as voidable; and thereby to ascertain whether the particular judgment supports or rejects the judicial bias hypothesis. Arguably, it is possible to assess the merits of shareholder *locus standi* and to establish whether the voidable characterisation was used by the FAC to deny the standing; and it is also possible to assess the merits of different constructions of the article 181 limitation periods and to ascertain whether voidable characterisation was used to arrive at the particular construction.

3.3.2 Knowledge attribution under article 181(2)

As previously explained, article 181(2) contains both the actual and a constructive standard for attributing the knowledge of the cause of action to claimants. Of the two standards actual knowledge is plainly the more ‘claimant-friendly’ standard for establishing the limitation period’s commencement date. If a claimant becomes aware that a transaction has been executed in breach of Part XI JSCA one year should be sufficient to file the claim, or at least to initiate protective proceedings pending fuller investigation of the facts. Enforcement of the Part would arguably become problematic only where the claimant learns of her cause of action at a time subsequent to when she should have learned those facts in the eyes of the court. In such cases there is a significant risk that the claimant would be barred from bringing her action especially given the limitation period of one year. From the investor protection perspective, therefore, actual knowledge would doubtless be the preferred standard for the courts to use.

Actual knowledge, however, has a considerable drawback in the efficiency terms. The drawback is unverifiability. Why the courts eschew the rules that condition on unverifiable information was explained in Chapter 2. In short, such rules lead to opportunistic behaviour *ex post*; and for this reason the parties themselves would not have bargained for them had they had the opportunity to do so (Schwartz, 1992). A claimant’s actual knowledge is unverifiable because it is within her exclusive control. Because claimants are the only true purveyors of their knowledge they would always maintain the lack of the relevant knowledge at such time that could lead to the dismissal of their claim under the statute.

The same applies to claimants that are juridical persons. Since a company's separate personality is artificial, it is capable of acting and knowing, as Davies points out, 'only if the acts or knowledge of human beings are attributed to it' (2002: 38).³¹ Actual knowledge would remain unverifiable even if the courts rely on the knowledge of constitutional organs that authorise legal proceedings, be it the board or the executive organ. It is unlikely for the board and senior management to act inconsistently with the wishes of the controlling shareholders. Thus, it can reasonably be expected that a claimant's board would deny any knowledge of the challenged transaction on their part at such time that would render the claim time barred by alleging absence of the requisite disclosure to the board. At the same time, the defendant counterparty could equally allege either that the disclosure was made and its fact is being concealed by the claimant in order to rescind the transaction or that, even absent the disclosure, the fact of the transaction was common knowledge and its particulars were always available to the board and senior management especially given their unhindered access to all of the claimant's internal books and records. In the context of companies' section 84 JSCA litigation, each party will be able to maintain opportunistically that the claimant found out that the transaction was carried out in breach of Part XI JSCA within or without the article 181(2) one-year period.

To avoid adjudication on the basis of unverifiable information courts would inevitably have to infer the claimant's knowledge from verifiable circumstantial evidence rather than ascertain what a claimant actually knew, and when. In practice therefore the article 199(2) petitions turn on the consideration of the verifiable circumstances that are presented in the parties' evidence and whether these are sufficient to construe the claimants as having been put on notice of their causes of action at a stage over a year prior to the bringing of their actions, in other words, on the interpretation of the constructive knowledge limb of article 181(2).

The following three sections focus on the circumstances that might be regarded as sufficient for this purpose from the efficiency perspective. The first argues that in actions involving solvent company claimants the only relevant circumstance is the date of the transaction's execution. In other words, the contract-based standard is the welfare maximising norm for attributing knowledge to claimants in company actions that involve solvent claimants. In the insolvent company cases, on the other hand, the second and third sections explore whether

³¹ For a broad overview of the variety of ways the knowledge and acts may attributed to a company see Davies, 2002: 38-59.

the only relevant circumstance to the application of article 181(2) is the date of appointment of an insolvency practitioner (the appointment-based standard) or also the contract-date, and if so, why. The analysis begins with the solvent companies and the contract-based standard, which, as was shown above, has been criticised in the literature.

Solvent claims: the contract-based standard

A convincing case can be made out that the contract-based standard offers the welfare maximising interpretation of article 181(2) in claims brought by solvent companies that are party to the transactions they seek to rescind. In these types of Part XI JSCA cases the contract-based standard has an efficiency advantage over any other interpretation of article 181(2) and this advantage also persists in relation to the article 181(1) ten-year limitations statute. In other words, the efficiency would have justified the FAC's use of article 181(2) and the contract-based standard even prior to the emergence of the SAC jurisprudence characterising related party transactions as voidable in the late year 2000.

The key reason for maintaining that article 181(2) and the contract-based construction of its knowledge provision is the welfare maximising statute of limitation in section 84 JSCA actions brought by solvent companies resides with the statute's capacity to mitigate the two problems set out in section 3.1.2 above namely, opportunism and damage to the interests of third parties. In addition, the statute offers savings in the adjudication costs, for the present purposes defined as expenses borne by the parties and the state in resolving disputes under Part XI JSCA,³² relative to other possible constructions of the article 181. These advantages all stem from the single fact that the contract-based article 181(2) statute provides for the shortest possible limitation period under article 181, which means that it would prevent the largest number of section 84 lawsuits brought by solvent companies. A reduction in section 84 lawsuits entails a reduction in the opportunistic lawsuits; a reduction in the instances where third parties suffer reliance losses resulting from the rescission; and (ultimately) a reduction in the number of disputes brought before the courts.

To be sure the statute is neither a perfect filter for opportunism, nor a conventional means to protect third party interests. Even if one year is a relatively short period for a transaction's dynamics to change and render it disadvantageous to the controlling shareholders,

³² In the law and economics literature adjudication costs are sometimes referred to as administrative costs. See Shavell, 2004: Ch. 12; Farnsworth, 2007: Ch. 6.

undoubtedly there will be instances where this is not the case. The contract-based article 181(2) statute would not stop all opportunistic claims and some transactions will be rescinded to the detriment of third parties. Importantly, however, nor would any other construction of the article 181 statute of limitations. The contract-based article 181(2) statute has an advantage over other constructions of article 181 because it is the statute that would prevent the greatest number of section 84 lawsuits.

That this is the case in relation to the article 181(1) ten-year limitation period is self-evident. But the same also holds true in relation to the alternative interpretations of article 181(2). Thus, it might be thought that a construction that required some showing of the board's or senior managements' knowledge of a disputed transaction and the conflict involved might offer a more accurate means to filter opportunistic lawsuits and to safeguard interests of third parties. After all knowledge of the relevant circumstances and a failure to promptly act on that knowledge might be the strongest indication of the lawsuit's opportunistic motives.

Knowledge of this sort, however, is unverifiable and judicially inaccessible even if the courts construe article 181(2) by reference to hard facts such as the presence or absence of documentation communicating the fact of the transaction and the conflict to the board. This is because such documentation would ordinarily be within the claimant company's possession or control. And it is rational, and hence very likely, for the company to deny the existence of the documents to avoid the dismissal of its action. For this reason any construction of article 181(2) that would require an article 199(2) petitioner to adduce positive evidence of the claimant's board's knowledge would likely result in the majority of the petitions failing. But even if in some cases defendants would manage to obtain and adduce evidence demonstrating that the claimant's board had the requisite knowledge at the time when the transaction was executed, these would still fall short in their number in comparison to the contract-based article 181(2) statute because under the statute the existence of the necessary knowledge at the time of execution is presumed in *every* case. Indeed, in presuming the presence of the knowledge and thus removing it as an issue between the disputants, not only would the statute attain the welfare gains associated with the reduced

number of the section 84 lawsuits but also it would carry further savings in the adjudication costs by lowering the average costs of the disputes.³³

This is not to suggest that the above advantages of the contract-based article 181(2) interpretation represent pure gains in the aggregate welfare. The potential welfare losses from the statute are also foreseeable. As with the gains, the likely losses originate from the fact that the statute would preclude more legal actions than any other construction of the article, which would likely capture genuine attempts to redress overreaching in the same breath with the opportunism. In other words, the statute would also likely have the greatest adverse effect on the deterrence of expropriation in comparison to other possible limitation statute under article 181. However, in the context of the Part XI JSCA litigation at the instance of the solvent companies it is highly likely that the losses would be, if not nonexistent then, negligible.

There are good reasons for believing that the welfare gains from the reduction of opportunism and from the improvement in the third parties' protection are likely to outweigh any losses from potential under-deterrence of insider overreaching. This should be apparent from the discussion in section 3.1.1 above. To recall, the section concluded that outside the financial distress situations companies were unlikely to offer a realistic prospect of enforcement of Part XI JSCA to remedy the controlling shareholder overreaching. It must follow then that any adverse effect on the deterrence from the inhibitions placed on such lawsuits would be at best marginal.

Furthermore, this contention is also applicable to a subset of the solvent company litigation that may have a more than marginal deterrence function namely, the actions to remedy expropriation at the hands of the rogue directors. Here, however, the economic argument is different. In Chapter 2 it was explained that the deterrence rationale for strong pro-investor rights and remedies was premised on the prohibitive costs involved in principals monitoring their agents. In these circumstances a low probability of misappropriation being detected results in the low probability of enforcement and hence in the deterrence deficit (Cooter and Freedman, 1991: 1048). Put differently, the enforcement effort (monitoring) is a central constituent of the deterrence and in the context of the control over the rogue director expropriation the monitoring costs are arguably not prohibitive.

³³ This is because there is one less issue for the parties to make submissions on and for the court to consider. On the reduction of adjudication costs by lowering average cost per claim see Shavell, 2004: 283; Cooter, 1985: 40.

Thus, as was emphasized in section 3.1.1 above, the controlling shareholders have both the access to the necessary corporate information and the incentives to detect the wrongdoing, the reason that lead a highly authoritative group of scholars to conclude that in the concentrated ownership companies managerial self-dealing ‘is not an issue’ (Kraakman et al, 2009: 178). Indeed, restricting the availability of the section 84 rescission for solvent company claimants to the first year from the transaction’s completion would create the efficient precaution incentives for the controlling shareholders to expend resources on the improvement of the internal control function until the marginal cost of the precautionary measures equals the reduction in the expected losses from the rogue director expropriation, the marginal benefit. The increase in the monitoring effort would in turn arrest the magnitude of under-deterrence (Cooter, 1985).

Notably, the application of the contract-based knowledge standard under article 181(2) does not rule out the rescission remedy altogether. It is not a blanket rule that shifts the losses on to the companies in all the circumstances, which is important. Third parties still face the rescission risk and the possibility of bearing losses on the unapproved related party transactions and, therefore, have the incentive to exercise precaution by, for example, screening transactions for conflicts of interests and taking ameliorative step to reduce the risk of restitution. In other words, the statute maintains the dual responsibility principle discussed in section 3.1.2 above and it arguably does so ‘at the margin’.

The statute’s allocation of the losses on transactions between companies and third parties may appear arbitrary. It determines *ex ante* that the third parties are the lowest cost avoiders of the losses on the unapproved transactions that are less than a year old and that the companies are the lowest cost avoiders of the losses on all other unapproved transactions. There isn’t room *ex post* for a court to reallocate a loss on to the third party from, for example, a blatantly expropriating transaction challenged two years post completion. Admittedly the loss allocation is crude. But it is intuitive and likely efficient.

First, if the company rescinds transaction within a year from the completion it is difficult to see what more it could have done short of preventing its occurrence altogether. The annual internal control, audit and reporting systems have performed their function. Second, if these systems did not detect the transaction within the year from the completion they would be

even more unlikely to detect it subsequently given the annual corporate reporting cycle. At the same time, longer time lapse from completion allows for more variables and volatility to alter the transaction's dynamics. Both factors suggest that the solvent company section 84 lawsuits that concern 'fresh' transactions are more likely to be brought to redress misappropriation and those that concern 'stale' transactions are more likely to be brought opportunistically. From this perspective the statute – in rescinding fresh transactions and allowing stale ones to stand – can be seen as allocating losses from misappropriation on to the third parties and from the unprofitable deals on to the companies and the controlling shareholders.

The alternative article 181 limitations statutes that were described above fail to achieve the dual responsibility at the margin in the analogous manner. Arguably, in extending the limitation period considerably beyond one year from completion, the statutes fail to create any meaningful precaution incentives for the companies while enabling them to externalize losses from unapproved related party transactions on to the third parties in circumstances where the same companies are better placed to prevent these losses.

In conclusion to this section it is also worth noting that the article 181(2) constructive knowledge and the RF Constitutional Court's tests implicitly direct the courts to the least cost avoider enquiry. The terms 'should have discovered' and the 'real opportunity to discover' invite the courts to consider the claimants' monitoring costs – the ease of access to the information on transactions and conflicts and whether the claimant took sufficient care to make a timely discovery of the transaction and the conflict it seeks to reverse. The contract-based article 181(2) statute presumption that controlling shareholders are well placed to detect expropriation by their appointee management within a fairly short period from its occurrence might seem overly harsh. But it is supported by the international scholarly community, as was emphasized above. And perhaps in legal environments where related party transactions cannot be rescinded automatically by virtue of doctrines such as bona fide purchaser there may well be little concern with the board-initiated litigation. However, in relation to the section 84 rescission suits the analogous provisions were not adopted until the SAC's June 2007 Decree No. 40; and were only expressly introduced into section 84 in July 2009. In these circumstances the short article 181 statute could offer a rule functionally equivalent to the more conventional doctrines that protect third parties' interests.

Insolvent claims: the appointment-based standard

The defensibility of the contract-based standard for attributing knowledge under article 181(2) is more difficult to maintain, both on the legal and economic grounds, when it comes to company lawsuits brought by the claimants under the control of insolvency practitioners. Yet, the case data discussed in section 3.5 below shows that the FAC has used the standard in such cases. To a large extent, as will be argued in the next section, developments in legislation and precedent explain the FAC jurisprudence. Also, these legal developments are not wholly without economic merit. In other words, the judicial bias hypothesis is not supported by this FAC jurisprudence. Prior to that discussion however, this section sets out why, but for the legislation and precedent, it is difficult to establish that the contract-based standard constitutes the welfare maximising application of article 181(2) in the insolvent company lawsuits brought under section 84 JSCA.

The difficulty arises because in insolvent company cases it is possible to construe an alternative interpretation of article 181(2) that the courts could use without conditioning its application on unverifiable information. This interpretation involves triggering the one-year limitation period upon the appointment of the insolvency practitioner but not sooner. For simplicity it will be referred to as the appointment-based constructive standard of attributing knowledge to claimants. Arguably, the appointment-based standard is the most claimant friendly, and therefore the most congruent with the investor protection principle, interpretation of article 181 in insolvency cases. Indeed, it can outlast even the ten-year article 181(1) limitations statute. Pursuant to the standard claimants would only need to submit that the insolvency practitioners had no, and could not possibly acquire, knowledge of transactions and conflicts prior to assuming their office in order to dismiss article 199(2) petitions. It is foreseeable that the article 199(2) petitioners would be unable to adduce evidence to the contrary and the disputes would be tried on their merits save perhaps for the most exceptional cases.

The availability of the appointment-based standard casts doubt over the efficiency of the contract-based standard. The reasons for this conjecture are twofold. First, as already noted, the appointment-based standard does not require the courts to consider unverifiable information. The appointment date is an observable and verifiable hard fact, which is difficult for the litigants to dispute. And it is unlikely that the administrators or liquidators would have any knowledge of the causes of the (subsequently brought) actions prior to their appointment. Therefore, there would be little scope for the courts to question the *bona fides*

of the claimants' submissions as to the lack of the relevant knowledge. Similarly, there would be little scope, if any, for the defendants, the article 199(2) petitioners, to make submissions to the contrary. Thus, the appointment-based standard reduces the average costs of the disputes in a comparable manner to the contract-based standard. It makes a presumption concerning the state of claimants' knowledge prior to the start of insolvency process and in doing so removes it as an issue between the disputants. Put short, the contract-based standard has no verifiability advantage over the appointment-based standard.

Secondly, the appointment-based standard has a clear advantage over the contract-based standard in terms of deterrence. The former allows insolvency practitioners a year to review internal books and records to identify wrongdoing and to bring proceedings against *any* transaction considered worth pursuing irrespective of its vintage. With the latter standard, on the other hand, the practitioners would only ever be able to challenge transactions that were executed within a year preceding their appointment. And even this is unlikely in practice because inevitably upon appointment time would have to be spent on the review of books and records thus increasingly foreclosing the possibility of rescinding transactions as time passes. It is likely therefore that the contract-based standard would result in heavier losses from its adverse effect on the deterrence and hence the greater potential for expropriation.

Furthermore, the magnitude of this effect in the insolvency claims is likely to contrast sharply with the solvent company actions where, as was explained above, the prospect of the Part XI JSCA enforcement to redress the controlling shareholder overreaching is highly fanciful. Ordinarily, as appointees and representatives of the creditors, insolvency practitioners are independent from controlling shareholders and management. Their decision to rescind a transaction is unlikely to be tainted by the conflict of interest. Therefore, the most credible threat of a company instituting proceedings contrary to the controlling shareholders' interests is likely to rest in the hands of insolvency professionals. Indeed, this was the conclusion in section 3.1.1 above, which also showed that the company law scholarship supports this proposition.

To be sure, the prospect of enforcement by an insolvent company is as remote as the prospect of insolvency. And for some controlling shareholders insolvency may seem too remote to offer a significant deterrent.³⁴ However, experience in Russia has shown such indifference to

³⁴ As Black, Kraakman and Tarassova noted over a decade ago, 'a controller who mostly self-deals will likely keep a potentially viable firm alive' (2000: 1751).

the prospect of insolvency to be misplaced. On the one hand, the precarious macroeconomic conditions, exemplified by the 1998 financial crisis, and reforms to the insolvency legislation have ensured a ‘remarkable’ increase in the bankruptcy applications over the period surveyed in this thesis (Oda, 2007: 207, 206 – 211). On the other hand, it has been extensively documented and widely reported that the insolvency procedures have become a potent means to effect hostile takeovers in Russia (Tavernise, 2000),³⁵ the process of involuntary change of control ordinarily considered impossible in countries with concentrated corporate ownership structure. Thus, reportedly in 2000 – 2001 up to 30 percent of insolvency cases processed by arbitrazh courts were initiated to facilitate hostile enterprise takeovers, an occurrence described by one commentator as ‘the most significant redistribution of economic assets since the voucher privatisation of 1993-1994’ (Volkov, 2004: 527).

Finally, it is possible that insolvency practitioners would seek to rescind every unapproved related party transaction that would bring net gains to the company irrespective of whether the transaction was executed at undervalue or whether it had lost its value since execution due to factors unrelated to misappropriation. Therefore, such suits could result in losses to the innocent third parties. In other words, as the shortest possible article 181(2) statute, the contract-based standard would retain an advantage over the appointment-based standard in terms of greater reduction of opportunism; greater protection of third parties; and greater savings in adjudication costs from the reduction in the total number of disputes brought before the courts. However, in cases arising from insolvency proceedings it is considerably less clear whether these benefits outweigh the losses from the greater potential for minority shareholder (and creditor) expropriation due to the contract-based standard’s adverse effect on the deterrence.

In particular, it is impossible to identify *ex ante* the party that could have avoided losses on unapproved transactions at the lowest cost with anywhere near the same degree of confidence as was expressed in relation to the solvent company cases above. Thus, to maintain that minority shareholders and creditors are the least cost avoiders *vis.* the third parties – a presumption that necessarily underpins the contract-based standard – one would have to be satisfied, as a minimum, that the minority shareholders and creditors are just as well placed to police the controlling shareholders as the controlling shareholders are to police their management.

³⁵ See also Oda, 2007: 207, 208 for an overview of the commentary.

Undoubtedly, this is impossible to maintain. While the minority shareholders are fully dealt with in Chapters 4 and 5, common sense suggests that they have neither the resources nor access to information to be in a position to perform monitoring at this level. Certainly there may be situations where it is plausible that the minority could have avoided losses on unapproved related party transactions at a lower cost than the third parties. Transactions and conflicts that are disclosed to the minority provide a good example. This, however, would require the court to investigate the circumstances of the transaction *ex post*, something that *prima facie* the contract-based standard does not allow for.

In summary, it is uncertain whether the contract-based standard would maximise the parties' aggregate welfare if applied to the insolvent company claimants. At the same time, it does not follow that the appointment-based standard is. This standard also allocates losses from the unapproved related party transactions *ex ante* save that here the losses would be borne by the third parties. There is no *a priori* reason to suppose that third parties are better placed than minority shareholders to avoid the losses. For the purposes of this thesis however, the appointment-based standard does not pose difficulties. It is congruent with the investor protection principle, which brings it outside the purview of the judicial bias hypothesis. The contract-based standard, on the other hand, is a clear departure from investor protection and, as suggested in this section, may not be justifiable on the efficiency grounds when applied to the insolvent company claimants at least without more.

The next section discusses the reasons why the contract-based standard may not support the judicial bias hypothesis even in insolvency cases. Before moving on, however, it is necessary to mention that it also may be difficult to reconcile the contract-based standard with article 181(2) and the Constitutional Court's 'real opportunity' test in insolvency cases. Thus, Telukina and Gabov have argued that the article 181(2) period cannot commence before administrators or liquidators are appointed (Telukina, 2005: 578, 579; Gabov, 2005: 373, 374). This is because the practitioners either cannot discover related party transactions completed in contravention of Part XI JSCA (Telukina, 2005: 578), or cannot realise the right to institute proceedings (Gabov, 2005: 374), prior to assuming competences of their office upon appointment. Both authors find support for their position in the SAC Judgment of 9

December 2003, which held that the limitation period could not commence before the institution of insolvency proceedings.³⁶

Insolvent claims: the contract-based standard

It is submitted that the contract-based standard may be the efficient interpretation of the limitations statute in the section 84 actions brought by companies subject to insolvency proceedings. Admittedly the ensuing explanation is intricate. But it is demonstrable.

The key reason for the above conjecture is that the contract-based standard does not foreclose entirely the rescission of unfair related party transactions by companies subject to an insolvency practitioner's control. A company could still seek rescission under insolvency legislation.

Thus, the Act on Insolvency (Bankruptcy) 1998³⁷ provided two gateways for the companies subject to insolvency proceedings to challenge related party transactions. The first was contained in section 78(1) of the Act, which empowered insolvency practitioners to challenge transactions executed by the debtor company on the grounds specified in the RF civil legislation and hence under section 84(1) JSCA. Section 78(2) of the Act provided the second gateway. The section empowered insolvency practitioners to challenge transactions involving conflict of interests 'if as a result of the performance of the said transactions losses were caused, or could be caused, to the creditors'. When the 1998 Act was replaced by the Act on Insolvency (Bankruptcy) 2002 in November of that year³⁸ the two provisions were retained in sections 103(1) and 103(2) of the 2002 Act.³⁹

The contract-based standard would not preclude the companies' ability to challenge related party transactions under section 78(2) of the 1998 Act and section 103(2) of the 2002 Act, provided, of course, the courts applied a different limitations statute under these two sections.

³⁶ *Постановление Президиума ВАС РФ от 9.12.03 No.12258/03*. Gabov, 2005: 373; Telukina, 2005: 578. Telukina, however, criticising the decision on the ground that the Court should have held more specifically 'upon appointment of the insolvency practitioner' rather than 'institution of insolvency proceedings' because an insolvency practitioner may be replaced by another practitioner who would have no relevant knowledge prior to the appointment (579).

³⁷ Federal Law No. 6-FZ of 8 January 1998.

³⁸ Federal Law No. 127-FZ of 26 October 2002. For an overview of the reforms of the insolvency legislation and the reasons behind it see Oda, 2007: 205-208.

³⁹ In both 1998 and 2002 Acts the relevant sections were contained in Parts dealing with administration rather than liquidation. However section 101 of the 1998 Act and section 129 of the 2002 Act specified that liquidators could also challenge transactions under these provisions.

An obvious outcome from this, is that the standard's negative effect on the deterrence is likely to be less pronounced. Under the insolvency provisions the claimants would have to demonstrate that losses were, or could be, caused to the creditors meaning that the costs of enforcement would likely be higher than in the section 84 claims where *prima facie* no evidence of losses was required to obtain rescission during the surveyed period. But even if higher enforcement costs entail weaker deterrence (Cooter and Freedman, 1991), the availability of the insolvency gateway still improves on the status quo in its absence.

More importantly, the requirement that transactions be loss-making facilitates courts to identify the least cost avoider *ex post*. In functional terms the requirement operates in much a similar manner to the conventional rules that protect the third parties and ensure dual responsibility at the margin referred to in section 3.1.2 above such as the good faith purchaser without notice defence. This is because whether or not a transaction was at undervalue or at overvalue is the sort of circumstance that would put the third party 'on notice' (Armour and Whincop, 2007: 456, 457). Farnsworth explains this reasoning neatly in the following paragraph (2007: 55):

'In the fraud case we say that the original owner loses if the later purchaser bought the goods in good faith and (what is pretty much the same thing) for their full market value. Assuming the buyer did his part, the original owner was indeed the least cost avoider. But if the price was suspiciously low, then we blame the buyer after all for being incurious or worse, and the original owner wins back the property. This shows how the idea of the least cost avoider can shed light even on cases where we want more than one party to be careful.'

In sum, the contract-based standard forces the insolvency practitioners to challenge related party transactions using the insolvency legislation rather than section 84 JSCA. And in doing so it forces the claimants to use provisions that enable courts to identify least cost avoiders *ex post* and to allocate the losses on transactions accordingly.

Furthermore, this outcome is also logical when considered from the creditor protection perspective, which is the proper purview of insolvency legislation. First, requiring insolvency practitioners to demonstrate that a transaction caused losses is congruent with a purpose of the legislation on voiding transactions that take place in the vicinity of insolvency namely, to safeguard the value of an insolvent company's assets for the implementation of

the statutory distribution process.⁴⁰ Second, protecting creditors from asset diversion on the basis of the presence or absence of a board or general meeting approval, which is the logical outcome of the insolvency practitioners seeking relief under the provisions of Part XI JSCA, is arguably an ill-advised policy. In financially distressed firms, and especially the firms with the concentrated ownership structure where the interests of the shareholders and the management are aligned, the risk to creditors from asset diversion stems precisely from the actions of directors and shareholders (Kraakman et al, 2009: 117, 118; Cheffins, 1997: 79).

Third, the contract-based standard would not exclude all the transactions completed in the vicinity of insolvency from rescission under section 84(1). The related party transactions performed within a year prior to the practitioner's appointment without the requisite Part XI JSCA approval would remain, at least in theory, voidable under section 84(1) at the instance of the company. As explained above, it is unrealistic to expect an insolvency practitioner to file for rescission on the day of her appointment. However, it is reasonable to suggest that one to six months is a sufficient period to examine a company's books and records for suspect transactions and to challenge their validity meaning that the transactions that took place up to eleven months prior to the appointment of the practitioner, if unapproved, could still be rescinded under section 84(1) and, hence, without establishing losses that would otherwise be necessary under sections 78(2) and 103(2) of the 1998 and 2002 insolvency legislation. In this way, the contract-based standard would in effect create a presumption that related party transactions carried out in the vicinity of insolvency were intended to put the assets beyond the reach of the creditors and were hence performed at undervalue or overvalue.

Thus, it is submitted, there is an arguable case that the contract-based standard is the welfare maximising limitations statute in the insolvent company actions that are brought pursuant to section 84(1) JSCA. However, the case is difficult to test because it rests on the courts (a) applying a more permissive limitations statute in lawsuits brought pursuant to sections 78(2) and 103(2) of the 1998 and 2002 Acts; and (b) using the requirement to demonstrate losses contained in those sections to identify the least cost avoiders in the fashion described above.

⁴⁰ See Mokal, 2005 describing this as a 'loss allocation norm' of insolvency law and stating that the UK equivalent of sections 78(2) and 103(2), namely section 238 of the Insolvency Act 1986, pursues this objective (311). In the UK section 238 requires that transaction be performed at *undervalue*. Section 4 of the US Uniform Fraudulent Conveyance Act 1918 similarly requires that 'the conveyance is made or the obligation incurred without a fair consideration'. See Clark, 1986: 40; Baird and Jackson, 1985: 830.

On the theoretical level, testing of the hypothesis would give rise to epistemological difficulties in that conclusions would have to be drawn with respect to one set of judgments based on the outcomes in a wholly different and unconnected set of judgments. On the practical level, it would involve an empirical assessment of a vast, and yet only indirectly relevant to the minority shareholder protection, jurisprudence. Indeed, as matters *prima facie* relevant to insolvency legislation and protection of creditors rather than the protection of minority investors and company law sections 78 and 103 were not covered by the sampling exercise.⁴¹

However, on 15 November 2001, Plenum of the SAC issued Decree No. 18, which proscribed the appointment-based standard and, in doing so, sanctioned judicial recourse to the contract-based standard in insolvency cases. The Decree was issued jointly with the Supreme Court to facilitate uniform interpretation of the Civil Code's limitation periods between the arbitrazh and general jurisdiction courts. Its 13th paragraph stated the following:

'When examining a petition by a party to litigation regarding the application of the limitation period in relation to a claim of a juridical person it is necessary to take into consideration that according to article 200(1) of the Civil Code the limitation period commences from the day when the juridical person discovered or should have discovered the infringement of its right. Taking this into account, the arguments of a newly appointed (elected) manager that he discovered the infringed right of the juridical person under its control from the moment of his appointment (election) cannot act as a ground for the alteration of the start of the limitation period, because in such cases the claim is to protect the rights of the juridical person and not the rights of the manager as a physical person. The same circumstance cannot act as a ground for a break in the limitation period.'

Notably, paragraph 13 states nothing about how the courts should interpret article 181(2) of the Code let alone that they should use the contract-based standard in actions involving insolvent claimants. There is no mention of article 181; no mention of a point in time when the limitation period is triggered; and there is no mention of insolvency or related terms such as liquidator. Nonetheless, the outcome of the paragraph was to authorise the use of the contract-based standard in the insolvent actions. Since the drafting of the paragraph is not explicit in this respect and because the interpretation suggested here runs contrary to certain

⁴¹ See section 1.2 above.

academic opinion, notably that of Gabov and Telukina mentioned at the end of the preceding section, it is worth setting out the argument in some detail.

First, although the paragraph refers only to article 200(1), it is similarly applicable to the interpretation of article 181(2). As was mentioned in section 3.2 above, article 197(2) of the Code requires special limitation periods to be interpreted in accordance with the general limitation period rules that are contained in articles 195, 198 – 207. Pursuant to article 197(2) therefore the courts must interpret article 181(2) consistently with article 200(1) and hence with paragraph 13 also. Although article 200(1) reference to *person*, as opposing to article's 181(2) *claimant*, perhaps leaves room for different and yet consistent interpretations;⁴² in claims brought by companies it does not because the juridical person whose rights are infringed is the claimant. Here the different wording in articles 181(2) and 200(1) is of no practical consequence.⁴³ In fact, it is not unusual to see the two articles treated interchangeably in the literature (Gureev, 2007: 129, 130) and in the FAC judgments in the case data.

Second, it is true that paragraph 13 only removes the inability of the new management to acquire knowledge of related party transactions prior to their appointment as a relevant factor in determining the commencement date under the limitations statute.⁴⁴ *Prima facie* the courts would still have to ascertain the point of time when the company, as a legal entity, discovered, or should have discovered, that a related party transaction took place without the requisite Part XI JSCA approval. As noted above, a company is capable of knowing only if the knowledge of human beings is attributed to it and it is possible that the relevant human beings, directors or senior management, also had no knowledge, or had no opportunity to acquire the knowledge, of a particular infringement of the Part prior to an insolvency

⁴² Plainly, in a dispute, the identity of the article 181(2) claimant and the article 200(1) person need not be the same. For example, a shareholder may bring an action derivatively to redress an infringed right vested in the company. In such circumstances it may be plausibly argued, as a matter of legal interpretation at least, that article 181(2) need not be construed in an analogous manner to article 200(1).

⁴³ It is difficult to see any material difference between the knowledge of 'the circumstances that provide the grounds for invalidating the transaction' under article 181(2) and the knowledge of 'the infringement of [the company's] rights' under article 200(1): the circumstances that provide the grounds for invalidating a related party transaction, namely the non-compliance with Part XI JSCA, arguably would be the same circumstances that would constitute the infringement of the company's rights.

⁴⁴ Interestingly the Decree justifies this by reference to the company's separate legal personality, which of course is a legal fiction. For arguments that judges invoke the separate legal entity concept for instrumental purposes see Whincop, 2001: 24 – 26; 45-66; Horowitz, 1992: 65-107.

practitioner assuming her office. Expressly paragraph 13 only proscribes the use of the appointment-based standard but does not go so far as to sanction recourse to the contract-based standard.

In reality, however, the outcome of paragraph 13 would remain analogous to that under the contract-based standard – the immunity for the related party transactions completed over a year prior to the replacement of a company’s management – even if the courts were to enquire into the knowledge of the outgoing supervisory board and senior management. The explanation is the same as was given above for why companies were unlikely to offer a realistic prospect of enforcement of Part XI JSCA to remedy the controlling shareholder overreaching outside the insolvency: the controlling shareholders, and their appointee management, are unlikely to cause a company to sue to rescind transactions that benefit these same controllers. The only difference here is that these controllers are no longer in office. However, if their knowledge counts for the purposes of the limitations statute then they would no doubt admit full knowledge of the relevant facts to protect the transaction with the article 181(2) time bar.

In itself the outcome may seem arbitrary.⁴⁵ It enables the wrongdoers to foreclose the possibility for the company to seek restitution on the basis of their submissions that they were fully aware of their wrongdoing. The paragraph’s recourse to the separate entity concept, and the jurisprudence that has reified it, appears if not as the plainest evidence of favouritism to controlling shareholders then certainly as a myopic exercise in the judicial formalism.⁴⁶ And yet it is functional and makes sense when considered in the context of channelling related party transaction disputes into the sections 78(2) and 103(2) of the 1998 and 2002 Acts jurisdiction. It is true that there is no mention of insolvency in paragraph 13, which might cast doubt over this explanation. However, there is sufficient evidence to make it credible. In particular, the following factors support the proposition that paragraph 13 was likely concerned with insolvent company actions and with directing such litigation into the

⁴⁵ Notably, in the UK a suit brought by a liquidator is subject to the same limitation period as would have applied if the suit was brought by the company, this being so despite the fact that liquidator brings the claim in his own name under s.212 of the Insolvency Act 1986 (*Eurocruit Europe Ltd, RE* [2007] 2 BCLC 598; see Davies, 2008: 607). However, the effect of the UK rule is less draconian since the limitation period is six years pursuant to section 2 of the Limitations Act 1980.

⁴⁶ See Whincop, 2001 observing that ‘[Judges] do their worst when they presume that suitable answers to doctrinal questions can be found by reifying the interests and intentions of the entity. Judges can only find in the corporate entity those attributes and capacities that they themselves invested it with’ (47).

jurisdiction of the insolvency legislation where a proof of losses is a prerequisite to restitution.

First, the Russian term ‘*rhukovoditel*’ used in paragraph 13 is sufficiently broad to encompass any person with executive competences of the company including insolvency practitioners⁴⁷ and from the knowledge attribution perspective it is difficult to conceive of a principled argument for disregarding the state of knowledge of one type of ‘new’ management and not the other. Secondly, in section 3.1.1 above it was explained that in Russia the post change of control litigation was unlikely to be prominent save for the insolvency cases where controlling shareholders cede control involuntarily and hence also their ability to influence litigation decisions of the new controllers. Thirdly, the Decree’s preceding paragraph, paragraph 12, was also concerned with litigation arising out of insolvency except where a company’s new management was collegial. Paragraph 12 introduced an analogous rule to paragraph 13 but in relation to liquidation committees – committees of creditors that could perform the functions of a liquidator without having the appropriate license pursuant to the 1998 Act’s simplified bankruptcy procedure.⁴⁸

But the clearest sign, however, was provided by the fourth factor namely, the development of insolvency legislation shortly following Decree No. 18. The Act on Insolvency (Bankruptcy) 2002 introduced a crucial distinction between sections 103(1) and 103(2), which was not present in sections 78(1) and 78(2) of the 1998 insolvency legislation that section 103 replaced. Section 103(7) of the 2002 Act stated that the claims brought under section 103(1) were to be brought by insolvency practitioners in the name of the company whereas claims brought under section 103(2) were to be brought by the practitioners in their personal capacity.⁴⁹

It is doubtful that the enactment of section 103(7) was a meaningless exercise in legal semantics. The section must have been passed in recognition that the applicable statute of limitations differed, or should differ, for sections 103(1) and 103(2). In particular, the

⁴⁷ Translations of *rhukovoditel* into English available on the online dictionary website www.multitrans.ru include: executive, manager, director, administrator, controlling person, and decision-maker. Available at <http://www.multitrans.ru/c/m.exe?CL=1&s=%F0%F3%EA%EE%E2%EE%E4%E8%F2%E5%EB%FC&l=1>. Accessed on 10 February 2014.

⁴⁸ Section 175(1.2) of the 1998 Act.

⁴⁹ SAC Decree No.32 of 30 April 2009 somewhat belatedly clarified that the company still had to feature in the proceedings but as the defendant. Belatedly because section 103 was repealed one month later when section 3(7) of the Federal Law No.73-FZ of 28 April 2009 came into force.

instruction that litigation pursuant to section 103(1) – the gateway for the section 84 JSCA actions – should be brought in the name of the company must have been passed with the paragraph 13 in the forethought. With the company as the claimant in such cases the legal consequence of the juxtaposition of article 181(2) and paragraph 13 would be the application of the contract-based standard precisely in the manner described above. In contrast, in requiring that the practitioner, rather than the company, act as the claimant under section 103(2), section 103(7) was taking the actions where losses had to be demonstrated outside the scope of paragraph 13. To achieve this effect without violating the requirement for consistency between articles 181(2) and 200(1), section 103(7) was taking advantage of the different terminology used in the two articles: the reference to ‘claimant’ in article 181(2) rather than ‘person whose rights are infringed’ in article 200(1). Since it is the claimant’s knowledge that is relevant to the application of article 181(2) and the company was no longer the claimant; its knowledge or that of its former management organs, would be irrelevant to the determination of the start of the limitations statute. The claimant insolvency practitioner, on the other hand, would be free to submit that she could not possibly discover the existence of a related party transaction prior to her appointment. Hence, the application of the appointment-based standard in the section 103(2) actions would be ensured.

In the author’s opinion it is simply impossible to interpret the 2002 reforms to the insolvency legislation in any manner other than the use of the contract-based standard to channel cases into the insolvency jurisdiction in order to allow the courts to review related party transactions on the basis of their value and economic merits, the activity that enables the courts to identify least cost avoiders *ex post* and to allocate the losses accordingly. Albeit this finer detail in the Russian insolvency legislation appears to have escaped the attention of the majority of commentators,⁵⁰ one perceptive author has considered the existence of section 103(7) and attributed it exactly to the different limitations statutes in the section 84 lawsuits where the proof of losses is *prima facie* unnecessary and the section 103(2) lawsuits where it is (Budylin, 2005: 24, 25).

It is also worth mentioning subsequent developments in the RF insolvency legislation. In 2009, section 103 was repealed and replaced with sections 61.1 – 61.9. Section 61.9 now states clearly that insolvency practitioners can challenge debtors’ transactions under the 2002 Act in the name of the debtor but with the limitation period calculated on the basis of the

⁵⁰ All the literature (save for one article) researched for the purpose of the thesis that discusses limitation periods in section 84 suits does not pick up on this point.

knowledge of the insolvency practitioner. It contains no reference to the claimants' capacity or knowledge in claims based on legislation other than 2002 Act. Perhaps this is because there is no equivalent to the former sections 78(1) and 103(1) that used to sanction insolvency practitioners recourse to the non-insolvency legislation such as the JSCA. In other words, the amended 2002 Act envisages the practitioners having recourse to the Act only.⁵¹

Finally, this reasoning is also supported by the same SAC Judgment of 9 December 2003 on which Gabov and Telukina rely in support of their arguments that article 181(2) limitation period cannot commence prior to the appointment of an insolvency practitioner is section 84 actions. Their reliance on the judgment is based on a misreading that has resulted due to their inattentiveness to the fact that article 181(2) could be construed differently under sections 78(1) and 78(2) of the 1998 Act. Had this been appreciated the authors would have perhaps played greater heed to the fact that the Court was adjudicating a related party transaction claim brought under section 78(2), as opposing to section 78(1), of the 1998 Act. This is plain from the Court's judgment, which expressly stated:

'According to subsection 2 of section 78 of the Federal Act 'on Insolvency (Bankruptcy)' a transaction of a debtor, completed by the debtor with an interested person, may be held by an arbitrazh court invalid upon application of the administrator, if as a result of its performance losses were or could be caused to the creditors. Consequently, the right to bring the current claim belongs only to the administrator. The running of the limitation period starts no earlier than the commencement of the administration process.'

In effect, the SAC was restating in respect of the 1998 Act what by then had already been achieved by section 103(7) of the 2002 Act. The practical outcome of the judgment, in relation to claims under the 1998 Act, and of section 103(7), in relation to claims under the 2002 Act, when considered alongside paragraph 13 of the Decree was to require insolvency practitioners to prove actual or potential losses from a related party transaction in order to obtain the rescission with respect to all such transactions save for those that occurred within the very vicinity of insolvency without a Part XI JSCA approval and that could be challenged in the section 84 JSCA suit.

⁵¹ Notably, section 61.2, which replaces the old sections 78(2) and 103(2), is considerably more sophisticated in protecting the third parties incorporating third party knowledge provisions and limiting the maximum age of transactions that could be challenge to three years. See also SAC Decree No. 63 of 23 December 2010 concerned with interpretation of sections 61.1 to 61.9.

3.4 Hypothesis

It is now possible to formulate the judicial bias hypothesis and to test it using the case data.

First, with respect to the section 84 rescission actions brought by solvent companies the economic analysis suggests that the contract-based standard is the more likely knowledge attribution norm to maximise aggregate welfare. Therefore, the FAC jurisprudence resorting to the contract-based standard would not support the judicial bias hypothesis.

As to the section 84 actions at the instance of the insolvent companies the efficiency case of the contract-based standard is, on the one hand, more subtle in contrast to the solvent company actions and, on the other hand, is impossible to falsify on the basis of the case data alone. However, the FAC judgments delivered after November 2001 that had used the contract-based standard would have accorded with the superior legal authority of the SAC Decree No.18. Thus, secondly, in the insolvent companies' actions, the FAC jurisprudence resorting to the contract-based standard that post-dates 15 November 2001 would not support the judicial bias hypothesis.

Given the epistemological difficulties with proving the efficiency of the contract-based standard in the insolvent companies' actions, it is less contentious to use a more conservative test in order to examine whether the case data does or does not support the judicial bias hypothesis. Thus, thirdly, only the FAC jurisprudence resorting to the appointment-based standard prior to November 2001 would be inconsistent with the judicial bias hypothesis. The less claimant friendly contract-based standard would, *arguendo*, support the hypothesis.

3.5 Case data

The FAC dismissed 25 cases brought by companies on the basis of statute of limitations. The cases represent 49 percent of all the company cases where the court declined to invalidate the transactions. The statute is the most frequent single ground for dismissals in company cases. It is fair to suggest, therefore, that the statute represents a considerable obstacle to these actions. Of course the descriptive statistics alone are insufficient to draw conclusions as to the judicial bias hypothesis and the ensuing discussion considers the FAC judgments in detail.

It is helpful to begin by drawing attention to two more general aspects of the FAC's statute of limitation jurisprudence in the companies' section 84 litigation before turning to the detail of the FAC judgments. The first point is that it appears that the jurisprudence has developed in a manner difficult to reconcile with the general thrust of the judicial bias hypothesis. The cases are open to an interpretation that the court had arrived at the contract-based standard following a transition from an initial position more congruent with investor protection. They suggest that the FAC's resort to the contract-based standard gained prominence only in 2001. In 1999 and 2000, the earliest two years when the FAC judgments could be obtained, the standard hardly featured in the FAC section 84 adjudication.

In this connection the year 1999 is of particular interest. Out of the six section 84 lawsuits where the FAC had considered article 181 that year only one, involving a firm under the control of a liquidator, was struck out under the article 181(2) contract-based standard.⁵² Importantly, and as will be shown below, the transaction was approved by the general meeting with the conflict of interest disclosed and without the conflicted party voting. In the other 1999 case to involve a liquidator in charge of the claimant and to turn on the statute of limitation the court found the disputed transaction to be voidable but held that the appointment-based standard, a standard congruent with the investor protection principle, was the correct interpretation of article 181(2).⁵³ In the remaining four cases the court struck down the lower courts' judgments for characterising the transactions as voidable and for applying the contract-based knowledge standard. It held that the void characterisation, and hence the article 181(1) ten-year limitation period, applied.⁵⁴ Notably, all the four actions involved solvent claimants where, as argued above, the efficiency case for the contract-based standard is at its strongest. It would appear therefore that in 1999 the FAC, in eschewing the contract-based standard in lawsuits brought by solvent claimants, was pursuing investor protection irrespective of the implications for the welfare maximisation. And it is also worth highlighting in this context that 1999 was the only year in the case data where the majority of judgments were delivered in the claimants' favour. *Prima facie* this is at odds with the contemporaneous criticism of the Russian judiciary, including that by the JSCA drafters, or

⁵² Постановление ФАС Московского округа от 27.10.99 по делу N. КГ-А40/3503-99 CDN16.

⁵³ Постановление ФАС Московского округа от 24.08.99 по делу N. КГ-А40/2657-99 CDN12.

⁵⁴ Постановление ФАС Московского округа от 5.05.99 по делу N. КГ-А40/1166-99 CDN4; Постановление ФАС Московского округа от 7.05.99 по делу N. КГ-А40/1257-99, Постановление ФАС Московского округа от 22.12.99 по делу N. КГ-А40/4212-99 CDN18; Постановление ФАС Московского округа от 26.07.99 по делу N. КГ-А40/2274-99 CDN7; Постановление ФАС Московского округа от 29.12.99 по делу N. КГ-А41/4350-99 CDN19.

with the criticism that has emerged subsequently but aimed at the experience in the late 90s (Black, Kraakman and Tarassova, 2000; Pistor and Xu, 2002; Radygin and Entov, 2003).

Furthermore, if the genesis of the FAC's article 181 jurisprudence was favourable to claimants under section 84 JSCA then assertions of judicial bias or incompetence are harder to maintain more generally because it is reasonable to expect such undesirable qualities to be entrenched. If, for example, the judges were corruptible and incompetent in 2001 and 2002, it is realistic to expect the same to have been the case in 1999 and 2000. And yet the case data suggests that it was not.

Secondly, the transition in the FAC's doctrine creates room for an alternative account for the ultimate prevalence of the contract-based standard in the court's related party transactions jurisprudence. The fact of the doctrinal shift makes it possible that the change was reflecting a swing in the court's attitude as informed by the judges' experiences with the Part XI JSCA litigation. The FAC may have come to doubt the worth of the companies' lawsuits brought under section 84 JSCA. Indeed, on this issue it has been said that courts have first-hand perspective (Coffee, 1985: 8). Litigation experiences and their perception by the judges might offer a more plausible explanation for the shift in the doctrine than a sudden affliction with corruption or indifference to the case outcomes on the part of the FAC judiciary.

From this perspective the early cases arguably become particularly important in that they inform the first judicial impressions of the related party transactions litigation and its merits. Thus, it was observed above that claims brought by insolvency practitioners represent 44 percent of all the actions brought by companies in the case data. And the descriptive statistics for the company lawsuits that failed under article 181(2) also appear broadly in line with this claimant pattern: during the surveyed eight-year period 12 out of 25 (48 percent) company claims that failed on the limitations statute were brought by companies subject to the insolvency practitioners' control. In other words, the distribution of the failed claims by the claimant type roughly reflects the distribution of the claimants in the total population of company claims. *Prima facie* this implies no predisposition in favour of a particular type of claimant on the part of the court.

However, there is a revealing difference if only the first four of the surveyed years (1999 – 2002) are considered. While the general claimant pattern was not markedly different – the insolvency claims comprised 44 percent of all company actions – of the 13 cases dismissed under article 181(2) in 1999 – 2002 only four (31 percent) involved claimants under the

control of insolvency practitioners. Moreover, two of the four cases involved transactions that occurred, or continued to occur, after the practitioners assumed their office.⁵⁵ In such ‘post-appointment’ cases, as will be suggested below, the economic analysis of article 181(2) is sufficiently similar to the analysis of the article in the solvent company cases to momentarily for the present purposes treat the two categories as one. Only two insolvency cases remain when this adjustment is made representing 15 percent of all the company lawsuits that failed under article 181(2) in 1999 – 2002.

The case data suggests, therefore, that the early development of the contract-based standard in the FAC’s Part XI JSCA jurisprudence appears to have occurred in the context of the cases brought by solvent companies, which is consistent with the predictions of the economic analysis set out in the earlier sections of this Chapter namely, that precisely in such cases the contract-based standard should prevail. Additionally, these early cases should also allay to some extent the epistemological concerns with testing the insolvent article 181(2) cases decided before the SAC Decree No.18 – there are only two such decisions in the case data.⁵⁶ The two cases along side others brought by firms under the control of the insolvency practitioners are considered next.

3.5.1 Insolvent cases

As observed above, of the 12 insolvent claims dismissed by the FAC under article 181(2) only two judgments preceded the SAC Decree No.18 dated 15 November 2001. In accordance with the formulation in section 3.4 the remaining 10 FAC decisions would not support the judicial bias hypothesis irrespective of the standard of knowledge the court employed in interpreting article 181(2) because the judgments post-date the Decree. Nevertheless, even if a detailed assessment of these cases is not necessary to test the hypothesis it is useful to consider the judgments in so far as they demonstrate the arguments advanced above. Prior to that, however, the two decisions that preceded the Decree have to be evaluated.

⁵⁵ *Постановление ФАС Московского округа от 14.08.01 по делу N. КГ-А40/4246-01* CDN47; *Постановление ФАС Московского округа от 18.07.02 по делу N. КГ-А40/4546-02* CDN68.

⁵⁶ *Постановление ФАС Московского округа от 27.10.99 по делу N. КГ-А40/3503-99* CDN16; *Постановление ФАС Московского округа от 14.08.01 по делу N. КГ-А40/4246-01* CDN47.

With respect to the two pre-Decree decisions only the appointment-based knowledge standard would be inconsistent with the hypothesis. Since, as will shortly become apparent, neither relies on the standard both judgments appear to support the hypothesis. However, this finding is *prima facie* only. A closer examination of their facts suggests that both cases are each in their own way exceptional and, as the discussion in the next paragraphs will seek to establish, sufficiently so to dismiss the hypothesis.

Постановление ФАС Московского округа от 27.10.99 по делу N. КГ-А40/3503-99 CDN16 is the earlier of the two judgments and is perhaps the most controversial. The liquidator's action to rescind a sale of property failed before both the first instance court and the FAC. In contrast to other judgments the FAC delivered in 1999 that involved the application of the limitations statute in the section 84 lawsuits, the court held that the related party transactions were voidable, thus attracting the application of article 181(2); that the one-year limitation period had commenced in December 1997 a day after the contract was executed; and that the period had expired by the time the claim was filed in July 1999. It appears therefore that the FAC was employing the contract-based standard to dismiss the liquidator's action. Furthermore, albeit the court did not address the question of the liquidator's knowledge – that it was unlikely the liquidator could have been aware of the company's cause of action prior to his appointment – it upheld the first instance's decision which expressly stated, '*the commencement of proceedings by the liquidator does not impact on the determination of the start of the limitation period because liquidators act in the name of the company-claimant*'.

The judgment is controversial because, as one of the earliest judgments in the case data, it appears to contradict the suggestion made above that the FAC was developing its statute of limitations jurisprudence from a pro-investor position. Furthermore, the court appears to have employed the contract-based standard in an insolvent company action where, as was also suggested above, the standard's efficiency advantages are less clear given the availability of the appointment-based standard on the basis of which to attribute knowledge to claimants under article 181(2).

And yet there are good reasons to maintain that the judgment's support for the hypothesis is more apparent than real. The principal among these is that the courts at both instances relied on a constructive knowledge standard other than the contract-based standard to reach their decisions despite the FAC's citation of the contract date as the limitation period's trigger.

The first instance judge held that the limitation period started in October 1997 when the general meeting was held and the resolution approving the sale and its price was passed without the conflicted party, a director, voting. It was also established from the meeting's minutes that the conflicting interest in the transaction was disclosed to the shareholders. The FAC upheld the lower judgment save for the start date of the limitation period. It thought the trigger date had to be the subsequent contract execution date in December 1997 because only at that point 'was the conflict of interest realised'. While it is arguable that the FAC's reasoning might have been erroneous – the company should have discovered the invalidating circumstances, a defective approval, at the point of the approval rather than at the point of execution⁵⁷ – it did not materially affect the outcome of the case.

Importantly, the way both courts construed knowledge differed from the contract-based standard. It is clear from the judgements that both courts were influenced by the disclosure at the general meeting rather than by the inability to determine which organs knew about the conflicted transaction and from what point in time. Under the contract-based standard the fact of disclosure of the relevant information is a wholly extraneous consideration to the determination of the start of the limitation period. The standard the courts in effect used – which for consistency this thesis will refer to as the 'disclosure-based standard' – will be fully elaborated upon in Chapter 5. It is sufficient to note here that, on the one hand, it is more investor 'friendly' than the contract-based standard and, on the other hand, it carries additional efficiency gains of information revelation to overtake the appointment-based standard in terms of aggregate welfare maximisation.⁵⁸

Furthermore, the facts gave rise to important concerns from the perspective of protecting transaction counterparties, albeit the judgments do not disclose the nature of the director's interest in the company that purchased the property making it impossible to determine how far it could be considered a third party. First, the infringement of Part XI JSCA that formed the substance of the liquidator's complaint was minor. At the time of the transaction, section 83.2 JSCA required non-conflicted members of the board, in addition to approving a transaction, to pass a resolution confirming that the consideration the company would receive

⁵⁷ The situation may have been different had the terms of transactions diverged from the terms approved by the general meeting but this was not the case on the facts.

⁵⁸ Of course, the disclosure was not made to the liquidator or the creditors and the courts in effect attributed the knowledge of the shareholders to the newly appointed liquidator via the separate entity concept. Such knowledge attribution gives rise to similar efficiency issues as the contemporaneous ownership rule analysed in Chapter 5.

would not be below the market value in accordance with section 77. Contrary to this requirement, the non-conflicted shareholders, not directors, passed the section 77 resolution at the general meeting.

It is fair to presume that the view of the disinterested board members would not have differed from the disinterested shareholders. This is because the transferor was a closed joint stock company which pursuant to section 7(3.2) JSCA could not have had more than 50 shareholders. Moreover, had the general meeting been used to outvote a shareholder-director that could have blocked the resolution if put before the board, doubtless the sale would have been challenged there and then by the shareholder rather than 18 months later by the liquidator. Indeed, the FAC observed *obiter* that the general meeting resolution complied with sections 77 and 83 JSCA. In other words, while the case was appealed and decided on the statute of limitations the FAC was evidently persuaded that Part XI JSCA was complied with in substance.

Secondly, and interestingly, the liquidator amended its claim to introduce section 78(2) of the Act on Insolvency (Bankruptcy) 1998 before the FAC. The FAC dismissed the claim under this head also but not on the limitation ground. Rather, it held that no evidence was tendered to show that the transaction caused or could cause losses to the creditors. It is also worth suggesting why the liquidator, and presumably the creditors in whose interests he acted, sought to judicially challenge a transaction that did not cause them any losses. The Russian financial crisis occurred in September 1998, which led to the devaluation of the rouble and high inflation. Annual inflation figures show that between July 1998 (six months after the property was sold in December 1997) and July 1999 when the claim was filed the Consumer Price Index in Russia rose by 126.31 percent.⁵⁹ Over this period the value of the property would have more than doubled and the restitution would have resulted in a significant windfall to the creditors. Put short, for the reasons offered above the judgment does not support the hypothesis notwithstanding the court not adhering to the appointment-based standard.

⁵⁹ CPI also rose between December 1997 and July 1998 but more moderately with monthly increases of between 1.5% and 0.10%. The annual inflation figure for the July 1998 – 99 period is available at <http://www.inflation.eu/inflation-rates/russia/historic-inflation/cpi-inflation-russia-1999.aspx>. The monthly inflation figures for the year 1998 are available at <http://www.inflation.eu/inflation-rates/russia/historic-inflation/cpi-inflation-russia-1998.aspx>. Accessed on 15 February 2014.

Finally, other FAC jurisprudence involving section 84 actions brought by distressed firms in 1999 suggest that the court's judgment was exceptional in the sense explained above. While five judgments involving liquidators were decided on grounds other than the statute of limitations, in *Постановление ФАС Московского округа от 24.08.99 по делу N. КГ-А40/2657-99* CDN12, delivered just over two months earlier, the FAC was clear in holding that the appointment-based rather than contract-based standard governed the interpretation of article 181(2) in cases involving insolvency practitioners. In this case, the claimant's liquidator challenged the validity of a loan provided by the defendant that also fell subject to the insolvency process by the time of the litigation. The parties had a common director but no section 83 JSCA approvals were obtained. The first instance court held the loan void. The appellate court reversed the decision on the ground that the loan was a voidable transaction and the one-year limitation period for bringing the suit applied. Since the transaction was executed in February 1998 but the claim was filed in March 1999 the interval for bringing the claim had finished.

The FAC upheld the first instance decision but on a different reasoning. The court construed article 168 and section 84 to mean that the Part XI JSCA transactions were voidable rather than void. However, in the court's opinion the claimant could not have discovered the circumstances invalidating the transaction prior to his appointment as the liquidator in February 1999. The court expressly rejected the argument that the claimant as a juridical person should have discovered these circumstances at the time of the transaction. In the court's view liquidators were not agents of the firms under their control and therefore acted in their personal capacity albeit for the benefit of others, namely the creditors. In other words, the FAC applied the appointment-based standard under article 181(2).⁶⁰ The case, therefore, affirms the proposition made above that the FAC's statute of limitations jurisprudence originates from a pro-investor protection position.

As to the second FAC decision to dismiss a section 84 suit brought by an insolvent company prior to the SAC issuing its Decree No.18, it was delivered almost two years later. In *Постановление ФАС Московского округа от 14.08.01 по делу N. КГ-А40/4246-01*

⁶⁰ Subsequently the SAC reversed the decision on the ground that the claimant lacked standing because it was not a party to the transaction (*Постановление Президиума ВАС РФ от 18.01.2000 No.6309/99*). The loan was assigned to a third party in March 1998 but the assignment was invalidated by a first instance court in the East Siberian circuit in January 1999 which prompted the litigation in the case discussed. However that decision was reversed by the East Siberian FAC in June 1999. The Moscow FAC appears to have proceeded without being aware of that decision.

CDN47 the parties entered into a settlement agreement on 6 December 1999 and had it sealed by the Moscow Arbitrazh Court (the ‘MAC’) three days later. The first instance and appellate courts, although rejected the defendant’s article 199(2) application, refused to invalidate the agreement on the ground that it did not constitute a transaction, no property having passed between the parties pursuant to it.⁶¹ The FAC struck down both judgments for construing the agreement to fall outside the scope of Part XI JSCA. Nonetheless, the court dismissed the liquidator’s action. It stated, ‘*[g]iven that the running of the period of limitation in a claim to invalidate a voidable transaction is calculated from the moment when the infringement of a right is discovered by the holder of the right – the juridical person, the start of the period cannot be made dependent on the question of who is carrying out the function of an organ of the said juridical person*’. Having observed that the claimant bank discovered the transaction no later than on 9 December 1999 when the MAC sealed the agreement, the FAC dismissed the action since it was filed outside the one-year period on 22 February 2001.

It is submitted the judgment does not support the judicial bias hypothesis notwithstanding the FAC’s clearest rhetoric eschewing the appointment-based in preference to the contract-based standard. The key reason for thinking this is that the outcome of the case would have been the same had the FAC applied the appointment-based standard in attributing the claimant bank with the article 181(2) knowledge. The MAC declared the claimant bank insolvent on 1 February 2000 and appointed the liquidator to his office on the same day. The claim would have been time barred also under the appointment-based standard.

Furthermore, and crucially, a closer reading of the judgment indicates that the FAC was applying the appointment-based standard in substance despite the *dictum* quoted above. The court disapproved of the liquidator’s delay in bringing the claim. It reviewed the chronology of the liquidator’s appointment and plainly thought he had a realistic opportunity to bring the claim earlier but had failed to do so. For example, the FAC criticised the two lower instances for accepting as the trigger date the date (15 March 2000) when the liquidator signed a deed assuming control over the bank’s property and documentation. The judgment is uncharacteristically emphatic in stating that even between March and December 2000 the liquidator had ample time to file his action.

⁶¹ The subject of the settlement was a waiver of the right to repayments of a loan.

The *dictum* might portray the court as unjustly harsh: it is not self-evident that eight months is sufficient to detect and contest a suspicious transaction – much would depend on the circumstances. But, on the one hand, the court’s interest in appointment dates alone and its concerns with the delay sit uneasily with the purely instrumental exercise of applying the contract-based standard. On the other hand, the judgment contains sufficient information to spot the court’s doubt that the action was not brought sooner for want of knowledge or inability to access documents. Specifically, the FAC pointed out that the same person acting as the liquidator was appointed as a temporary administrator of the bank in November 1998 in accordance with the supervision process mandated by the Act on Insolvency (Bankruptcy) 1998 and had remained in that position until his reappointment as the liquidator. The fact that the liquidator was appointed as such in February and then signed for the documents in March 2000 was extraneous to his ability to detect the transaction.⁶² It is this fact that underpins the whole of the judgment. In substance, the FAC was applying the appointment-based standard of a sort save that the contract date was the only logically possible date to set off the limitations statute – a trigger date in November 1998 would have led to the statute’s expiry before the conclusion of the settlement agreement in December 1999.

Arguably, the post-appointment cases – the cases where transactions take place after the appointment of the insolvency practitioner such as the instant case – have more in common with the solvent company cases than with the regular, pre-appointment, insolvency cases. The economic rationale for the contract-based standard in the post-appointment insolvency cases is analogous, if not stronger, to the rationale in the solvent cases.

First, courts face similar difficulties in ascertaining the claimant’s knowledge for the purposes of article 181(2). The lack of the insolvency practitioners’ knowledge of the transactions, and the circumstances pointing to their invalidity, is difficult to verify when the transactions take place ‘on their watch’. The appointment-based standard’s verifiability virtue namely, the impossibility of acquiring knowledge prior to the appointment, is absent in the post-appointment cases. Indeed, in the instant case the court’s scepticism of the

⁶² Under the 1998 Act, the temporary administrator was subject to a duty to protect the debtor’s assets and was endowed with extensive powers including the right to challenge transactions; the right to request any information on the debtor’s affairs from the directors, who were obliged to honour such requests; and the right to petition a court to remove non-cooperative directors (sections 60 and 61). Although the Act permitted management to remain in charge of the firm during the process, subject to restrictions on certain corporate actions, the court had the discretion to transfer all management powers to the temporary administrator if the directors did not act to preserve corporate assets or impeded the actions of the latter (section 58).

liquidator's ignorance was not wholly misplaced given that the settlement agreement was subject to the MAC's approval – the settlement was scarcely concealed.

Secondly, circumscribing the insolvency practitioners' ability to challenge transactions that take place after they assume office creates the efficient precaution incentives for the practitioners to prevent the dissipation of assets subject to their oversight. Arguably, there is greater strength to the contributory negligence type arguments in relation to insolvency practitioners because their core function is to safeguard the companies' assets for the benefit of the creditors. And it is telling when, in criticising the liquidator for failing to bring the claim sooner, the FAC explicitly set out the temporary administrator's powers and duties contained in sections 60 and 61 of the 1998 Act. The court clearly thought that the agreement should have and would have been discovered at the time it took place but for the liquidator's failure to exercise his powers and neglect of his duties while acting as the temporary administrator. Therefore, the second pre-Decree No.18 case also does not support the judicial bias hypothesis notwithstanding the court's reliance on the contract-based standard in its judgment.

At this juncture it is fitting to mention *Постановление ФАК Московского округа от 18.07.02 по делу N. КТ-А40/4546-02* CDN68, which demonstrates the similarities between the solvent and post-appointment insolvency cases well. In addition, although the decision postdates Decree No.18, the FAC's interpretation of the law might be considered disagreeable. The claim was brought by the Government Corporation ARCO, an organisation set up pursuant to the Act on the Restructuring of the Credit Organisations 1999 with the task of investigating and restructuring banks following the 1998 financial crisis.⁶³ Section 17 of the Act empowered ARCO to challenge the validity of transactions completed in contravention of the civil legislation by credit organisations three years prior to ARCO assuming the control over the organisation. The FAC dismissed ARCO's action on the ground that article 181 of the Civil Code is the imperative norm regulating limitation periods in suits to invalidate transactions and that the article does not contain any derogations.

However, it is very likely that the court was prepared to circumscribe section 17 in this manner only because ARCO was slow in challenging the transaction. The transaction in

⁶³ Federal Act No.144 of July 1999. Although ARCO sued in its own name, it was in control of the distressed bank SBS-AGRO since November 1999. The lawsuit could have been brought in SBS-AGRO's name and indeed the bank supported ARCO's submissions at the appellate instance and before the FAC.

dispute was an IT support agreement the defendant bank had entered into in January 1999 and had had it renewed in 2000. The claim, however, was only filed in January 2002. Since ARCO took control over the bank in November 1999, the courts at all the three instances did not encounter any difficulties in applying the appointment-based standard to dismiss ARCO's action. Here, in contrast to the preceding case, the application of the standard was not problematic because the one-year period would not have expired before the occurrence of the transaction. Nonetheless, the case offers a good demonstration because ARCO argued that it had only discovered the agreement in November 2001 when it carried out an independent valuation of the support services provided under the agreement. The courts rejected the submission because the agreement was renewed in 2000 after ARCO assumed control. Additionally, the receipts executed by ARCO acknowledging that the services were carried out were produced in evidence.

Thus, as with the earlier post-appointment case, the dispute highlights, on the one hand, the difficulties in verifying claimants' knowledge and, on the other, that there is room to take more efficient precaution by the newly appointed insolvency practitioners and, perhaps, a role for the law to engage those incentives. Effectively, the court interpreted section 17 and article 181(2) as allowing ARCO to challenge transactions that took place up to three years prior to its appointment provided the lawsuits are opened within a year from ARCO taking office. To the extent limitation periods play a role in reducing the delay and legal uncertainty in imposing time limits on bringing the claims once a person becomes aware of an infringement of her rights, the judgment is difficult to object to. Indeed, an unqualified interpretation of section 17 would have granted ARCO unlimited period of time to challenge transactions and resulted in an unjustifiable situation from the perspective of counter-parties to these transactions.⁶⁴ Finally, in this case the transaction was pre-existing, albeit continuing, making it unnecessary for the court to resort to the contract-based standard. However, had the transaction took place wholly after ARCO coming into office, it is likely

⁶⁴ It is notable that the FAC has applied the appointment-based standard and not a contract-based standard in other litigation involving ARCO that appears in the case data. ARCO, ultimately successfully, filed to rescind a pre-existing transaction within a year from its appointment and had the FAC used the contract-based standard it would have led to the dismissal of the case. See *Постановление ФАС Московского округа от 10.05.01 по делу N. КГ-А40/2167-01*, *Постановление ФАС Московского округа от 19.02.03 по делу N. КГ-А40/200-03-II*, *Постановление ФАС Московского округа от 4.12.03 по делу N. КГ-А40/9674-03-II* CDN104. The case was appealed to the FAC three times and to the SAC once on various grounds including the statute of limitations. See also *Постановление ФАС Московского округа от 24.05.01 по делу N. КГ-А40/2518-01* CDN42.

the FAC decision would have resembled the earlier judgment and rightly so given the comparable circumstances to the solvent cases.

The first ‘regular’ insolvent section 84 claim to be dismissed by the FAC under the contract-based standard did not emerge until October 2002, almost a year after the SAC Decree No.18. In *Постановление ФАК Московского округа от 2.10.02 по делу N. КГ-А41/6504-02* CDN74 both the first instance court and the FAC declined to invalidate a sale of property under section 84 JSCA. Although the claimant was subject to liquidation, enabling the courts to use the appointment date as the limitation period trigger, the contract date, December 2000, was used to time bar the claim. The FAC’s *ratio* is thin on detail beyond stating that the first instance court applied the relevant legislation correctly. However, it does recite the substance of the first instance judgment one aspect of which is interesting. The claim was based on section 78(2) of the 1998 Act, as well as Part XI JSCA, and the first instance held that the section was not proved. The substance of the section 78(2) claim was that the property was transferred in exchange for bonds with a call date in 2006 and that their current valuation was below par – not that the transaction was originally at an undervalue. To some extent the case supports the broader arguments presented above that the intended effect of the contract-based standard in the section 84 lawsuits was to channel the insolvency cases under the insolvency legislation where the undervalue of the transaction was a precondition to the rescission, albeit that the 2002 Act would not come into force for almost another month. The contract-based standard jurisprudence in the FAC’s Part XI JSCA adjudication involving insolvent claimants was already settled by the time the 2002 Act came into force.⁶⁵

However, the real impact of the use of the contract-based standard in the insolvency Part XI JSCA cases became marked only in 2003, two months after the reforms to the insolvency legislation took effect. Whereas, as highlighted at the start of the section, in 1999 – 2002 period the insolvency claims, while comprising 44 percent of all company actions, had a disproportionately successful pass rate on the statute of limitations ground: of the company actions that were time barred during that period the insolvency cases only represented 31 or 15 percent depending on how the post-appointment cases are treated. In the 2003 – 2006 period, while again comprising 44 percent of all company actions, the insolvency claims had

⁶⁵ See *Постановление ФАК Московского округа от 23.01.02 по делу N. КГ-А40/8298-01* CDN58 where the FAC had invalidated a transaction on grounds unconnected with Part XI JSCA but held that the lower instance court erred in also applying the Part because it was unavailable due to the contract-based limitations statute.

a disproportionately unsuccessful pass rate under the statute of limitation representing eight out of 12 (67 percent) company actions that failed on that ground.

During these last four years of the surveyed period only three cases brought by the insolvency practitioners managed to surmount the statute of limitations: in two cases the FAC invalidated the transactions and in one case the invalidity was refused but on a non-procedural ground. One of the three cases was successfully brought by the Government Corporation ARCO, which, as explained above, operated under the statute of limitation outside the regular insolvency legislation regime.⁶⁶ In another case the claimant filed the action within the contract-based article 181(2) one-year limitation period. The challenged property transfers were completed in November and December 2002 respectively and the claim was filed approximately six months later in July 2003. The FAC held the contracts valid on the ground that the general meeting of shareholders approved the transactions in the summer of 2002.⁶⁷

The third case, however, is the most interesting. *Постановление ФАС Московского округа от 15.05.06 по делу N. КГ-А40/3360-06* CDN156, provides compelling support for the proposition that Russian courts and policy makers were attempting to direct the related party transactions litigation involving distressed firms under the insolvency legislation. The courts at all the three instances invalidated the transaction despite it taking place in September 2001 some three years prior to the filing of the claim in October 2004.

⁶⁶ The FAC delivered three judgments in the dispute. In the second of the judgments, *Постановление ФАС Московского округа от 19.02.03 по делу N. КГ-А40/200-03-II*, the FAC sent the lower courts' decisions for a retrial on several grounds stating, *inter alia*, that pursuant to section 17 of the Federal Law on Restructuring of Credit Organisations ARCO could not discover circumstances indicating invalidity of a transaction prior to its appointment. The judgment followed previous litigation on the matter, *Постановление ФАС Московского округа от 10.05.01 по делу N. КГ-А40/2167-01*, where the courts at all the three instances held the transaction, a loan assignment, void on a number of grounds including the breach of the JSCA related party transactions approval requirements. The cases were reversed by the SAC (*Постановление Президиума ВАС РФ от 26.04.02 No.7030/01*) and sent for a retrial on several grounds including for holding the assignment void rather than voidable. The SAC decision was followed by the litigation discussed at the beginning of the footnote. Ultimately, following a third retrial, the assignment was invalidated by all the three instances, *Постановление ФАС Московского округа от 4.12.03 по делу N. КГ-А40/9674-03-II* CDN104.

⁶⁷ *Постановление ФАС Московского округа от 28.02.05 по делу N. КГ-А40/900-04; Постановление ФАС Московского округа от 5.10.05 по делу N. КГ-А41/9300-05* CDN145. The liquidator unsuccessfully argued that the approval should have been obtained from all the non-conflicted shareholders rather than from the non-conflicted shareholders that were present and voting.

The contract-based limitation period was overcome because the liquidator brought the action in her personal capacity pursuant to section 103(7) and pleaded under sections 103(2) and 129(4) of the 2002 Act. The absence of the requisite approval under the JSCA was cited in support of the claim, and hence the case appears in the case data, but was not part of the substantive pleadings. The judgment does not discuss the statute of limitation but it is plain that the appointment-based standard was complied with: the liquidation proceedings were opened in April 2004 and the claim was filed in October 2004. However, it is likely that had the claimant relied solely on Part XI JSCA the contract-based article 181(2) would have time barred the claim.

Perhaps more surprising is the courts' contentment that the transaction which took place over two years prior to the claimant being declared insolvent (April 2004) caused losses to the creditors. The facts go some way towards justifying such a finding. The transferred property was a 100 percent shareholding in a company, which held 60 percent share in a sports complex development in Moscow. The development was valued at 458 million roubles in June 2000. In July 2005, the Moscow City Government, the owner of the remaining 40 percent of the project, compulsorily acquired the remaining 60 percent for 811.5 million roubles. Despite the fair value of the company in September 2001 being somewhere between these two sums it was sold for 7000 roubles – its nominal value. The director and 50 percent shareholder in the seller also held 70 percent shareholding in the acquirer. On this basis, the FAC held that the lower instance courts were correct to find that the sale was intended to siphon off the claimant's assets in the vicinity of insolvency, which subsequently led to a substantial reduction in assets available to creditors and caused losses to the debtor.

The eight cases decided against the insolvency practitioners further support the argument. *Постановление ФАС Московского округа от 2.11.05 по делу N. КГ-А40/10317-05-П-Б* CDN147⁶⁸ provides the best illustration of the policy to restrict the insolvency practitioners' reliance on the JSCA. The challenged transaction, a sale of property, was already subject to unsuccessful litigation under the insolvency legislation where it was decided, on the basis of an independent valuation, that the property was sold at the market value and therefore did not cause losses to the debtor or its creditors.⁶⁹ Thus, a claim founded on Part XI JSCA was the only avenue left to the liquidator to rescind the transaction. The first instance and appellate

⁶⁸ The case came before the FAC twice. The first judgment is *Постановление ФАС Московского округа от 27.12.04 по делу N. КГ-А40/11700-04*.

⁶⁹ *Постановление ФАС Московского округа от 21.10.04 по делу N. КГ-А40/9027-04*.

courts invalidated the transfer under the Part. The FAC struck down the decisions and sent the case for a retrial. On retrial, the first instance court invalidated the transaction; the appellate court reversed that judgment; and the FAC upheld the decision of the appellate court.

The FAC's reasoning in its two judgments is instructive. In its first judgment the FAC sent the case for the retrial on the ground that the lower instance courts could not adequately determine whether the limitation period had expired without a determination regarding the start of the period: the moment when the claimant's relevant organ found out of the conflict of interest or the moment when that was discovered by the liquidator. In particular the courts failed to establish whether the liquidator brought the claim in his personal or, in the debtor's, corporate capacity. The FAC observed that the claimant was relying on section 81, 83 and 84 JSCA, which indicated that the claim was brought under section 103(1) of the Act on Insolvency (Bankruptcy) 2002. However, according to section 103(7) of the Act, a liquidator could bring claims in his/her personal capacity only under subsections (2) – (5) of section 103.

In its second, and final judgment, the FAC upheld the decision of the appellate court stating that the court correctly applied articles 181 and 200 of the Civil Code in finding that the limitation period began to run from the date of the contract and had expired by the time the claim was filed.⁷⁰ The first instance court's finding, that the liquidator could not discover the transaction prior to his appointment, was held to be irrelevant to the application of the law.

The appellate court's decision, the FAC approved of, is also instructive. First, the court expressly applied paragraph 13 of the SAC Decree No.18 in reaching its conclusion that the liquidator's knowledge, or lack thereof, was irrelevant to the determination of the start of the limitation period. Secondly, the court explicitly cited the FAC's previous judgments in analogous cases involving liquidators to justify its interpretation of the law on the ground that such construction of the statute of limitations was reflected in the established FAC case law.

The next four cases are interesting because the claimants relied on both the JSCA and the Act on Insolvency (Bankruptcy) in their pleadings to rescind the transactions. The judgments support the argument that the courts were channelling the litigation into the insolvency legislation. The FAC, while time barring the JSCA claims under the contract-based standard,

⁷⁰ Also interestingly, the displaced non-conflicted members of the claimant's board submitted that they knew the transaction involved a conflict of interest.

had reached its conclusions on the separate insolvency legislation grounds. In *Постановление ФАС Московского округа от 23.04.03 по делу N. КГ-А40/718-03* CDN83 the FAC upheld the lower courts' decisions, which held that the challenged contract, executed in January 1999, could not be challenged under section 84 JSCA because the limitation period had expired from the date of the contract. The court also upheld the lower tier judgments time barring the claim under the insolvency legislation. Importantly, however, under the latter ground the liquidator's appointment date, May 2001, was used to trigger the period, which had also expired since the claim was filed in July 2002. In other words, the contract-based article 181(2) standard was used in the section 84 claim and the appointment-based standard was used in the section 78(2) claim.

In *Постановление ФАС Московского округа от 17.06.03 по делу N. КГ-А40/3840-03-П* CDN85⁷¹ and *Постановление ФАС Московского округа от 17.06.03 по делу N. КГ-А40/3766-03* CDN86 are two separate cases brought by a temporary administrator against one and the same defendant bank, also subject to insolvency proceedings, seeking to invalidate two loans the bank provided to the company subject to the administrator's control in February and October 1997 respectively. Having held that the limitation period for challenging the loans under the JSCA had expired, the FAC also held that for the purposes of the insolvency legislation the administrator had failed to demonstrate how the claim was addressed at protecting the creditors' interests or that it would result in restoration of the claimant's property.⁷² Similarly in *Постановление ФАС Московского округа от 30.04.04 по делу N. КГ-А40/3026-04-2* CDN122 the FAC declined to invalidate the transaction, a sale of property, on the grounds that, first, the limitation period had expired for the purposes of the JSCA; and, secondly, that the transaction did not infringe the rights and interests of the creditors for the purposes of the insolvency provisions.⁷³ Notably, the FAC expressly

⁷¹ *Постановление ФАС Московского округа от 26.09.00 по делу N. КГ-А40/4349-00* was the first FAC decision to examine the February 1997 loan. The FAC sent the case for retrial to ascertain whether the claimant received the funds.

⁷² In both the cases the facts established that the claimant received the funds under the loan agreements. Even if the loans were held invalid the claimant would have to repay the principal and interest due under the unjust enrichment provisions of the Civil Code. For this reason the use of JSCA to invalidate loans has been criticised as nothing more than a delaying tactic (Dobrovolskii, 2006: 274).

⁷³ The FAC rejected the liquidator's argument that the sale infringed the rights of the creditors because the transaction was executed in March 2000, two and a half years prior to the liquidation petition being filed with the court. In addition, the liquidator did not establish that the sale was carried out at a loss to the company: the property was privatised in February 2000 and resold at that price (\$500,000) a month later.

observed that the special rights available to the liquidators when it came to the question of the attribution of knowledge for the statute of limitation purposes under the insolvency legislation did not extend to the claims brought under the general civil legislation outside the Act on Insolvency (Bankruptcy).

Finally, in the remaining three cases a breach of section 83 JSCA approval process was the sole claim ground for invalidating the transactions. The FAC applied article 200 of the Civil Code in reaching the conclusion that the change of the claimants' management did not affect the claimants' knowledge for the purposes of establishing the start of the limitation period, which, in the respective cases, the court found to have expired since the date of the transactions.⁷⁴

3.5.2 Solvent cases

In 13 of the 25 company cases that failed on limitations ground the claimants were solvent. In these cases the FAC's use of the contract-based standard in applying article 181(2) does not support the judicial bias hypothesis as expressed in section 3.4. Nonetheless a closer look at the jurisprudence is instructive.

The discussion of the cases in this Chapter began with an observation that the early development of the contract-based standard in the FAC's Part XI JSCA jurisprudence appears to have occurred in the context of the cases brought by solvent companies, which is consistent with the predictions of the economic analysis. This proposition is illustrated and supported by the descriptive statistics already referred to and by the preceding discussion of the insolvent company cases. The solvent company cases compliment this analysis by bringing to light the facts on which the economic rationale for the contract-based standard is premised: difficulties in ascertaining knowledge; incentive for precaution; opportunism; interests of the third parties.

⁷⁴ *Постановление ФАК Московского округа от 21.10.03 по делу N. КГ-А40/8200-03* CDN98 (contract date July 2000, claim filed April 2003); *Постановление ФАК Московского округа от 21.10.03 по делу N. КГ-А40/8244-03* CDN99 (contract date April 2000, claim filed April 2003); *Постановление ФАК Московского округа от 28.08.03 по делу N. КГ-А40/6214-03* CDN92 (contract date October 1998, claim filed April 2001). In the latter case the transaction was carried out with the 99 percent shareholder and was approved by the remaining one percent non-conflicted shareholder.

Thus, the first FAC judgment in the case data to dismiss a solvent company action under the statute of limitations demonstrates these points well. *Постановление ФАС Московского округа от 12.01.00 по делу N. КГ-А40/4449-99* CDN20, albeit not the first case in the case data to apply article 181 to dismiss claims, was the only time barred action before the FAC in 2000. Briefly, the dispute involved the following facts.

In October 1995 the claimant purchased a number of shares in itself on the secondary market from third parties. In December 1995 and October 1996 these shares were sold to the first defendant. In December 1998 the first defendant sold the shares to the second defendant. The claimant sought to rescind all the transactions on the ground that the original share sales were not approved by its board in breach of section 83 JSCA as both the claimant and the first defendant had a common director.⁷⁵ Since the first defendant did not acquire good title to the shares, it was argued, the sale to the second defendant was also invalid. In defence, the second defendant pursued, *inter alia*, an article 199 petition. In response, the claimant submitted first, that only the first defendant could issue the petition; and secondly that in any event its board had no knowledge of the transactions because the initial share sales were not reflected in the company's register of shareholders. The courts at all the instances found the petition to have been made correctly and the article 181(2) limitation period to have expired.

Albeit *dicta* are silent on how the courts attributed the claimant with the knowledge, there is sufficient information in the judgments to illustrate why the courts may have been tempted to apply the contract-based standard and would have been justified in doing so on the efficiency grounds.

First, the facts offer a good illustration of the difficulties in ascertaining the knowledge of the claimant's board. Unsurprisingly, the claimant submitted that its board was not aware that the shares were sold to the first defendant – the board thought that the shares were held in treasury at its disposal. Yet, certain matters must have cast doubt over the claimant's averred ignorance of the transaction for the courts. Thus, section 72(3) JSCA permits companies to hold shares in treasury only for a period of one year whereupon such shares must be cancelled in accordance with the procedure specified in the section. The second share sale to the first defendant in October 1996 was executed three days before the date when the shares were bought back from a third party a year earlier. It is likely that the timing of the two sales

⁷⁵ The judgments do not state the date when the claim was filed. However, case documents contain an interlocutory ruling dated 27 April 1999 freezing the disputed property. On this basis it is possible to conclude that the claim would have been filed at some stage during the first quarter of 1999.

was due to the desire to avoid setting off the cancellation process under section 72(3) rather than purely coincidental. Thus, if the claimant's board knew that the company held shares in treasury,⁷⁶ and that, if the shares were not resold, the board would have had to summon general meeting to cancel the shares and to obtain reduction of capital approval from the shareholders it is highly likely that the board was also aware of the sale taking place. But even if the board was not aware of the share sales to the first defendant, arguably it should have discovered that the shares requiring cancellation were missing from its treasury in late 1996. Put short, contrary to the submissions from the claimant, the circumstantial evidence indicated that the board must have known of the sales to the first defendant at the time they took place.

The likelihood that the claimant's board was in fact aware of the sales to the first defendant but did not challenge them at the time they took place ties in with other reasons in favour of the judicial recourse to the contract-based standard under article 181(2). Thus, secondly, opportunism is apparent from the facts and was implicitly picked up on by the first instance court in its judgment. The likelihood that the December 1998 share sale prompted the litigation indicates that the suit was motivated by the claimant's attempt to exercise control over the composition of its shareholder body rather than by the desire to redress harm (likely fanciful given the impending cancellation of the shares held in treasury pursuant to section 72(3)) to its investors from the share sales to the first defendant. And it is the reluctance to invalidate the December 1998 share sale that informs the outcome of the judgment to exempt the earlier share sales to the first defendant from scrutiny by the court. The reluctance instantiates the policy that the shareholders, at least in public companies, should be able to transfer their shares free from encumbrances imposed by the company or other shareholders (Davies, 2002: 21-24) – a policy that is undoubtedly crucial for the emergence of stock markets. The first instance court was explicit on this point. It stated that pursuant to section

⁷⁶ Apart from submissions that the board thought the claimant held the shares, section 72(2) permits board of directors to purchase shares on the secondary market under certain conditions without seeking approval from general meeting. The validity of the buy-back transactions was not challenged by the company, which suggests that the board authorised the purchase. It is also highly doubtful that the board had no knowledge of the shares being purchased into the treasury because, if that was indeed the case then, there could not be any complaint against the third party registering the shares, presumably the act that triggered the litigation.

7(2) JSCA shareholders of an open joint stock company could alienate their shares without obtaining consent from other shareholders.⁷⁷

Finally, the imperative to safeguard the interests of third parties in cases that involve sale-purchase of shares in open joint stock companies scarcely needs mentioning especially where the development of markets for corporate stock is the openly proclaimed policy goal of the JSCA. The second defendant did not make any submissions as to the knowledge, or otherwise, on the part of the claimant's board of the share sales. It is likely the second defendant was in no position to make them. It is reasonable to suppose that, as a purchaser from the first defendant, the second defendant could not know of the conflict of interest between the claimant and the first defendant; whether that conflict was disclosed; or indeed that the shares in the claimant that it was buying from the first defendant had been acquired from the claimant some two and a half to three years earlier.

In contrast to the first two years, 2001 and 2002 saw a considerable increase in company cases dismissed pursuant to the statute of limitation. Eight of the 13 solvent company cases dismissed under article 181(2) were dismissed by the FAC during the period. As with the case above, the facts in all the eight cases demonstrate traits that support recourse to the contract-based standard.

Thus, in *Постановление ФАК Московского округа от 8.02.01 по делу N. КГ-А41/114-01* CDN38 and *Постановление ФАК Московского округа от 5.03.01 по делу N. КГ-А41/708-01* CDN39, two cases involving the same characters but different contracts, the FAC, having established that the contracts were executed in February 1998 and November 1997 respectively, dismissed both claims under the contract-based article 181(2) standard because they were filed outside the one-year period in October 2000. However, in both cases it was manifest that whatever might have caused the delay it could not have been a lack of knowledge or an inability to acquire it.

The reason for this resides with a third case *Постановление ФАК Московского округа от 29.12.99 по делу N. КГ-А41/4350-99* CDN19 that involved the same parties and protagonist and that was decided by the FAC almost a year earlier. In that case the FAC voided a transfer of property on the ground that the claimant's director held 36 percent shareholding in

⁷⁷ The FAC approved the judge's reliance on section 7(2) JSCA. In 2001 the section was amended to expressly state that the company, as well as the shareholders, have no right of first refusal in circumstances when a shareholder in an open joint stock company sells his/her/its shareholding.

the transferee and had failed to obtain the requisite Part XI approvals for the transfer. The instant cases challenged two construction subcontracts with the same defendant company and on the same grounds. However, given that the claimant's board discovered the director's conflicting interest at least by August 1999, when the original lawsuit was filed, it is not farfetched to assume that the directors ought to have reviewed other transactions between the two firms and challenged them at that point.⁷⁸

In the next two cases the disputants were also the same save that they were disputing two different transactions. The facts make it apparent that both cases arose from an inter-group dispute than from a concern to obtain relief for shareholders prompted by a sudden discovery of self-dealing expropriation. In the earlier case, *Постановление ФАС Московского округа от 18.04.01 по делу N. КГ-А40/1673-01* CDN41,⁷⁹ the FAC declined to invalidate an agreement to sell property dated 13 April 1998 because the claim was filed on 21 April 2000, over a year since the agreement. It was doubtful that the agreement was not challenged sooner for lack of knowledge of the transaction or conflict. As to the conflict, the FAC established that the conflicted directors had notified the claimant's board of their conflicts – cross-directorships at both firm party to the litigation – in September 1997. The court also noted that this conflict could also be ascertained from the defendant's charter documents. But perhaps the most betraying fact was that the claimant was OAO VNIIDMASH ('the OAO') and the defendant was ZAO VNIIDMASH ('the ZAO'). It would have been a tall order for the claimant's board to maintain that they thought the agreement was with an independent third party.

As to the ignorance of the transaction, here too the court was sceptical. It noted that the transfer of title was registered with the Moscow's City Property Registration Committee and that the claimant's manager signed an order acknowledging the transfer. More importantly, however, the property was located on the same premises as the claimant's office and was used by the defendant's employees following the agreement. In short the court was satisfied

⁷⁸ Another interesting feature from a more general judicial bias perspective of the cases is that two of the three judges that had heard and dismissed the claimant's appeals in 2001, also were on the three-judge panel that heard and resolved in the claimant's favour the 1999 case.

⁷⁹ The case followed a previous decision of the court to retry the case for insufficient investigation of evidence by the lower courts (see decision *Постановление ФАС Московского округа от 11.10.00 по делу N. КГ-А40/4591-00*).

that the claimant's board knew of the transaction and the conflict of interest therein from the date of the contract.⁸⁰

In the second of the two cases, *Постановление ФАС Московского округа от 24.07.01 по делу N. КГ-А40/3779-01* CDN45⁸¹, the FAC dismissed the action to rescind a provision of services agreement executed in December 1999 on the ground that the OAO filed its claim out of time in February 2001. As with the two cases described above, the claimant's OAO lack of knowledge was betrayed by its previous litigation with the ZAO. Thus, the litigation to rescind the contract for a breach of Part XI JSCA was actually initiated by the ZAO and won on the ground that its board did not approve the contract ('the original proceedings').⁸² The OAO unsuccessfully opposed that litigation arguing that the agreement was valid. The first instance decision was delivered in January 2001. In response, the OAO issued a fresh claim in February 2001, the subject matter of the instant FAC judgment asking the court to rescind the agreement and compel ZAO to repay RUB 254,400 outstanding for the services already performed ('the subsequent proceedings'). In March 2001, the first instance court dismissed the subsequent proceedings under the statute of limitations. Shortly after this decision, the OAO appealed the original proceedings to the FAC asking the court to rescind the agreement for the future only, because, with services having been performed, restitution was impossible. The FAC accordingly amended the first instance decision to rescind the agreement only for future services. Subsequently, the subsequent proceedings were dismissed by the appellate instance in May 2001 and by the FAC in July 2001 on the ground that article 181(2) limitation period had expired.

⁸⁰The facts of the case were somewhat extraordinary with the claimant taking good title to the property as the ultimate outcome. In fact the parties executed three agreements in relation to the disputed property. The first was the agreement discussed above to transfer property concluded in April 1998; the second was an agreement in June 1999 to nullify the transfer of property agreement, and the third was an agreement in November 1999 to nullify the June 1999 agreement. Although all the agreements were executed under the same circumstances the claimant, perhaps unsurprisingly, only challenged the first and the third. Since the claimant filed suit in April 2000 the first agreement could not be challenged but the third could and accordingly the court invalidated the last agreement. The court refused to make a restitution order because no property passed under the invalidated contract. However, given that the June 1999 agreement to nullify the property sale still stood, the claimant could take good title under it. Indeed, the claimant did just that by registering transfer of title to the property with Moscow's City Property Registration Committee. The defendant challenged the registration of claimant's title but unsuccessfully (*Постановление ФАС Московского округа от 4.03.02 по делу N. КГ-А40/918-02*). The facts highlight the rather arbitrary outcomes that might result when the access to Part XI JSCA relief is governed by limitation periods. The facts, however, were exceptional.

⁸¹ The same agreement involving the same litigants was already considered by the FAC once *Постановление ФАС Московского округа от 16.04.01 по делу N. КГ-А40/1653-01*.

⁸² *Постановление ФАС Московского округа от 16.04.01 по делу N. КГ-А40/1653-01*.

The OAO's defence to ZAO's article 199(2) petition is nothing short of bizarre. The earlier litigation discussed above had already established that the cross-directorships were disclosed to the OAO's board in 1997 leaving only the absence of the knowledge of the transaction itself as a viable ground to argue that the claimant had no knowledge of the infringement of its rights for the purpose of article 181(2). Thus, the OAO argued that its board had only learned of the agreement in March 2000. In evidence, OAO offered minutes from its board meeting dated 3 March 2000 that showed the board discussing the question of the agreement being executed without its approval. The FAC dismissed this evidence holding that pursuant to article 181(2) the OAO knew of the transaction from the day of the agreement.

The court's decision is understandable. Even taking the minutes at their face value they only show that the OAO board, having discovered an irregularity in the execution of an agreement, instead of refusing to perform and seeking to invalidate it, allowed the OAO to carry out the services and then proceeded to defend the agreement through the courts when ZAO issued its section 84 proceedings in a bid to avoid payment. In other words, the board's conduct was at odds with its self-proclaimed role as the defender of its shareholders from self-dealing expropriation. Arguably, the litigation had more to do with a falling out of commercial parties over an agreement they were initially content with and then using section 84 JSCA to renege when the relationship, for whatever reason, went sour.

In the last two solvent company cases that were time barred by the FAC in 2001, the court's judgments do not discuss the statute beyond stating that the lower courts had applied it correctly. The challenged agreements were completed in 1998 and 1999 but the claims were not initiated until 2001. It is impossible to say from the judgments what submissions were made concerning the parties knowledge and hence to ascertain whether the courts had used the contract-based standard. However, the facts show again that the court would have been correct to apply the standard. The cases are wholly unrelated to each other but in substance involved analogous disputes: both disputes were started by the 'defendants' issuing proceedings to enforce outstanding debt; in both cases the 'claimants' counterclaimed that the initial loans were invalid for non-compliance with Part XI JSCA; in both cases it was established that the claimants received the funds pursuant to the loan agreements.⁸³ In these kind of cases, to repeat a former FAC judge Dobrovolskii cited above, section 84 proceedings

⁸³ *Постановление ФАК Московского округа от 14.08.01 по делу N. КГ-А40/4184-01* CDN46; *Постановление ФАК Московского округа от 21.12.01 по делу N. КГ-А40/7393-01* CDN56.

achieve little more than delay the repayment that would ultimately follow under the unjust enrichment provisions if the loan is invalidated (2006: 274).

While admittedly the true causes cannot be known, it is interesting that following the 2001 litigation there is a change in the judicial rhetoric. The court is more expressive of its impatience with the solvent company cases that are filed out of time under the contract-based article 181(2) period. It begins to articulate the contributory negligence – efficient precaution type of argument, albeit couched in the legal discourse of the JSCA interpretation. Thus, in *Постановление ФАС Московского округа от 7.08.02 по делу N. КГ-А40/5080-02* CDN70 an attempt to rescind a November 1999 property sale with section 84 proceedings in December 2001 failed on the statute of limitations before all three instances. In this case, the board's knowledge of the transaction was not in dispute. It was approved in a June 1999 meeting where eight of 11 board members were present and voted in its favour. Rather, the claimant submitted that three conflicted directors voted at the meeting without disclosing their shareholding in the transferee in contravention of section 82 JSCA. Their failure to disclose the conflict, it was argued, also entailed that the board, and hence the claimant company, could not know of the circumstances indicating the transaction's invalidity at the time it was executed for the purposes of article 181(2).

The FAC disagreed. It held that the board must have known of the conflict both at the time of the vote and subsequently when the transaction was completed. The court relied on the following facts to doubt the claimant's submission. First, the claimant company held a ten percent stake in the transferee, which pursuant to section 65 JSCA requires board approval. The directors must have known of the identity of the defendant's other shareholders from the moment when the defendant was incorporated and could not have thought that they were transacting with an unrelated third party at the time of the property sale. Second, the evidence produced before the court included a joint venture agreement executed between the claimant, the three directors, the claimant's other shareholders, the defendant and the defendant's members, which identified the directors as having shares in the defendant and the extent of their shareholding. Having recited the evidence, the court, in one short sentence, laid the ground to throw the question of the boards' knowledge of conflicts into irrelevance. It stated, '*Moreover, in accordance with section 93 of the Act on the Joint Stock Companies, joint stock companies are obliged to keep track of their affiliated persons and to produce an account on them in accordance with the legislation of RF*'. It followed, the court went on to say having cited the dates of transaction and proceedings, that the non-disclosure of conflicts

to the board cannot in itself act as a ground to dismiss the article 199(2) petition. Put differently, the court clearly thought it was the responsibility of the controlling shareholders to keep tabs on conflicts under their control.

Six days later, an entirely differently constituted FAC delivered *Постановление ФАК Московского округа от 13.08.02 по делу N. КГ-А40/5213-02* CDN71. The decision completes the rationalisation-legitimisation process of the contract-based standard application in solvent company cases that had begun in the preceding judgment. Here, the court extended the controllers' responsibility for the oversight of transactions as well as conflicts. The case concerned the rescission of a loan provided to the defendant company on the ground that its director was conflicted and the transaction did not receive the requisite approval. In response to the article 199(2) petition, the claimant firm submitted that it lacked the requisite article 181(2) knowledge – its shareholders could not have discovered the transaction because it was not reported in the annual accounts. According to the claimant the funds were moved in February 1999 but their absence was not discovered until May 2001.

The FAC held that the claimant should have discovered the transaction, and the fact that it was carried out in breach of JSCA, at the time it took place. It thought the lower courts, in rescinding the loan, erred in ascertaining when the claimant discovered the transactions for the purposes of article 181(2) rather than when it should have discovered it. The FAC observed that pursuant to section 85 JSCA a joint stock company is required to carry out an audit at least once a year or at any other time upon an initiative of the internal audit committee. The claimant therefore should have discovered the loan as early as the annual reviews for the years 1999 or 2000. Furthermore, the court observed, section 93 JSCA required firms to maintain a register of its affiliated persons; to keep the register open for the shareholders; and disclose it in the annual reports. The FAC concluded with a *ratio* that speaks volumes for the purposes of this thesis:

'The circumstances established by the [lower instance] court apparently evidencing that in fact the company, personified by its relevant organs, found out about the execution of the disputed transaction in May 2001, only demonstrate the absence of the requisite accountability processes and control over the activity of its employees and organs rather than that the claimant should have found about these circumstances after two or three years after they took place.'

Of 14 solvent company cases that were heard by the FAC in 2003 – 2006 only four failed on the statute of limitations in 2003 – 2006.⁸⁴ The judgments are scant in their reasoning for applying the one-year limitation period.⁸⁵ However, in all the four cases, the courts at all the three instances agreed that the limitation period had expired. Evidently the FAC and the lower courts were strictly adhering to the doctrine developed during the earlier period. Of the ten cases that were not time barred all but two were brought within the one-year from contract date period.⁸⁶

Conclusion

This Chapter set out to appraise the FAC statute of limitation jurisprudence in section 84 JSCA lawsuits to rescind the related party transactions. The legal and economic analysis carried out in this Chapter facilitated a formulation of the judicial bias hypothesis in section 3.4. The subsequent evaluation of the case data in section 3.5 showed it to be inconsistent with the hypothesis. The primary early development of the contract –based article 181(2) knowledge standard occurred within the courts jurisprudence arising from the claims brought by solvent companies. In this circumstances the efficiency rationale for the standard is the

⁸⁴ *Постановление ФАС Московского округа от 5.10.04 по делу N. КГ-А40/8874-04* CDN130 (contract in March 2002; claim filed in March 2004); *Постановление ФАС Московского округа от 24.01.05 по делу N. КГ-А41/12661-04* CDN136 (contract in January 2002, claim filed in June 2003); *Постановление ФАС Московского округа от 25.05.06 по делу N. КГ-А40/4607-06* CDN157 (contract in July 2002, claim filed in March 2005); *Постановление ФАС Московского округа от 20.06.06 по делу N. КГ-А40/5526-06* CDN159 (contract in November 2002, claim filed in November 2005).

⁸⁵ In *Постановление ФАС Московского округа от 25.05.06 по делу N. КГ-А40/4607-06* CDN157 the FAC did state that the claimant should have discovered the circumstances indicating invalidity of the transaction within the one-year period from the date of the contract because pursuant to sections 82, 85, and 93 JSCA it was the responsibility of the claimant to maintain the relevant information. In other words, the formulation had survived the test of time at least to the extent it is possible to draw that conclusion from the limited date range of the case data.

⁸⁶ In the two cases the defendants did not make an article 199(2) application (*Постановление ФАС Московского округа от 6.06.05 по делу N. КГ-А40/4439-05* CDN140; *Постановление ФАС Московского округа от 24.04.03 по делу N. КГ-А40/2198-03-Б (retrial)*, *Постановление ФАС Московского округа от 18.06.04 по делу N. КГ-А40/2169-04-П (final)* CDN125. In the remaining eight cases the invalidity was obtained in *Постановление ФАС Московского округа от 8.12.03 по делу N. КГ-А40/9796-03* CDN107; *Постановление ФАС Московского округа от 24.12.03 по делу N. КГ-А40/10273-03* CDN108; *Постановление ФАС Московского округа от 18.07.06 по делу N. КГ-А40/6004-06* CDN161; *Постановление ФАС Московского округа от 3.10.06 по делу N. КГ-А40/9441-06* CDN165. The four cases that failed on the substantive grounds were *Постановление ФАС Московского округа от 22.05.03 по делу N. КГ-А40/3275-03* CDN84; *Постановление ФАС Московского округа от 11.11.03 по делу N. КГ-А40/8835-03* CDN101; *Постановление ФАС Московского округа от 20.06.06 по делу N. КГ-А41/5280-06* CDN132; *Постановление ФАС Московского округа от 20.06.06 по делу N. КГ-А41/5280-06* CDN158.

strongest. The application of the standard in the insolvency cases on the other hand becomes noticeable only in 2003 following the legislative developments, which have signalled the death knell of the appointment-based standard. In other words, in relation to the insolvency claims there was no support for the judicial bias hypothesis on the basis of a combination of both legal and economic factors. Finally, the earliest cases feature a strong pro-claimant judicial stance a finding also inconsistent with the judicial bias hypothesis.

In addition, the descriptive statistics for 2003-2006 period raise some interesting questions. Eight out of 14 (57 percent) solvent company cases had overcome the contract-based one-year statute, which stands in contrast to the three out of 11 ratio (27 percent) in the insolvent cases. The relatively high ratio of meeting the contract-based standard in the solvent company cases is surprising. To be sure, it would be a far cry to suggest that the shift in the FAC's jurisprudence towards a more restrictive interpretation of the statute has led to adoption of more effective internal control processes by Russian firms. The data is hardly sufficient.

However, it is also doubtful that the contract-based doctrine dissuaded the out of time claims from being pursued through the courts. Given the low cost of litigation in the Russian commercial courts,⁸⁷ many claims would retain a positive net present value to the controlling shareholders, or their lawyers, to make the out of time litigation worth a shot. Intuition suggests that there ought to be more solvent company actions failing on the contract-based standard.

As Chapter 5 will show, this intuition is correct. A large number of claims that should have been brought by the companies have instead been filed by their shareholders. In these cases the companies appear as the defendants but make substantive submissions in support of the claimant – in reality running the claim but in the name of the shareholder so as to avoid the strict statute in the companies cases. The phenomena and its implications are explored in Chapter 5.

Finally, the ability of a number of the solvent company claimants to challenge the transactions within the one-year limitation period is reassuring. It indicates that the task is not impossible – effective internal control systems can and, as the cases demonstrate, do detect suspicious transactions within sufficient time to bring lawsuits before the courts. In

⁸⁷ The topic explored further in Chapter 4 pages 138, 139.

other words, the contract-based standard set by the FAC is not so high as to provide a complete bar to cases brought by the solvent companies.

CHAPTER 4

SHAREHOLDER *LOCUS STANDI*

Introduction

This and the next Chapter are concerned with the procedural rules in shareholder Part XI JSCA suits. This Chapter examines the merits and pitfalls of permitting individual shareholders to litigate under the Part and the Russian legislature's and the FAC's responses to the problems pertinent to the shareholders' *locus standi*.

Few commentators, if indeed any, dispute the necessity for some kind of shareholder enforcement mechanism of related party transactions rules. Even the more vociferous US critics of the derivative suit (a common law mechanism for the enforcement of fiduciary duties by individual shareholders (Kershaw, 2009: 538)) like Fischel and Bradley accept that shareholder enforcement plays an important role at least in deterring the more 'egregious derelictions by corporate management' (Fischel and Bradley, 1985: 286, 287). The acceptance of the need for the shareholder enforcement is not surprising. It was observed in Chapter 3 that persons in control of a company are unlikely to cause it to sue to rescind transactions that benefit these same persons. To reiterate Parkinson's point cited at the beginning of that Chapter, the effectiveness of related party transactions rules depends on there being an agent independent from controlling shareholders and management that is able to enforce these rules.

However, as will be shown below, commentators also invariably accept that the individual shareholders' right to bring proceedings on behalf of companies should not be unfettered (Davies, 2002: 249, 250; Kershaw, 2009: 539). Minority shareholders, albeit independent from companies' controllers, as holders of small stakes in a company have little incentive to consider the effect of a legal action on other shareholders who are supposed to benefit from the action as well as bear its costs (at least the costs incurred by the company in defending the suit). In particular, there is a danger that the action may be pursued irrespective of its effect

on the company's value, as long as the action appears to have a positive net value to the claimant shareholders, or their legal representatives (Easterbrook and Fischel, 1991: 101). The choice between the two imperfect enforcement agents – companies under the control of the alleged expropriators and shareholders with small stakes in these companies – is a tough one and, as Easterbrook and Fischel put it, commands no ready answer (Easterbrook and Fischel, 1991: 106). What seems clear, however, is that some control mechanism is necessary to ensure that shareholder actions benefit companies and that jurisdictions frequently adopt such mechanisms of one sort or another.¹ The more common approaches to controlling shareholder litigation vary from forbidding shareholders from initiating certain types of suit² to 'collectivising' shareholder enforcement through the imposition of minimum ownership thresholds (Grechenig and Sekyra, 2007) and/or subjecting the right to proceed with the claim to judicial review (Davies, 2002: 250; Clark, 1986: 646, 647).

A review and analysis of the merits of different approaches and their suitability in Russia, whether on the investor protection or efficiency grounds, is beyond the scope of this thesis. The purpose of this Chapter, and the one that follows, is more modest. In accord with the thesis's objective of appraising the FAC adjudication, the Chapters seek to ascertain what constraints in the form of the procedural rules the FAC has imposed on shareholder actions under Part XI JSCA during the surveyed period, including the complete bar to such claims; to assess whether, and in what circumstances, the constraints are defensible from the perspective of the judicial bias hypothesis (i.e. on the grounds of a higher order legal authority, congruence with the investor protection principle, or the Kaldor-Hicks efficiency); and to appraise the FAC adjudication against these normative criteria.

This Chapter is structured as follows. Section 4.1 discusses the difficulties of conferring minority shareholders with the right to enforce related party transactions rules. Section 4.2 examines legislative provisions on *locus standi* to ascertain whether and to what extent the legislation permitted individual shareholder standing under Part XI JSCA during the eight-year period surveyed in this thesis. Subsequently, it examines the FAC case data to ascertain whether the court has allowed minority shareholder actions. Having established the fact of the individual shareholder standing in the FAC jurisprudence, the following Chapter turns to

¹ See for example, Davies, 2008: 609-614; Easterbrook and Fischel, 1991: 105, 106; Kershaw, 2009: 538, 539; Parkinson, 1993: 245-259; Reisberg, 2007: 83, 84.

² Davis, 1985 noting the New York case law that restricted standing to sue to void transactions to company initiated actions only (50).

the analysis of the rules that constrain individual shareholder enforcement that have featured in the jurisprudence.

4.1 Problems with minority shareholder enforcement of Part XI JSCA

The problems that beset the minority shareholder enforcement of related party transactions rules are well documented in the literature. It is helpful to treat these problems as falling into two categories. The first set of problems goes to the issue of why minority shareholder litigation may lead to a suboptimal level of enforcement of related party transaction rules even in circumstances where the standing rules are ‘claimant friendly’. There are reasons to believe that even if individual shareholders with a holding as little as one share are permitted to sue under Part XI JSCA not all legal actions that ought to be brought will be brought. The second set of problems goes to the issue of why minority shareholder litigation may lead to claims being brought in the circumstances where they ought not to be brought. As indicated earlier, there are concerns that minority shareholder suits carry the risk of being contrary to the interests of the company and its shareholder body as a whole. And it is these concerns that underpin the arguments against unfettered minority shareholder enforcement rights. Each set of problems will now be dealt with in turn.

4.1.1 Suboptimal enforcement problems

Apart from legal encumbrances, which vary with jurisdictions, corporate law scholarship identifies two principal problems that may result in inadequate enforcement of related party transaction rules by the minority shareholders. These are the limited access to information that may reveal a cause of action and the insufficient incentives to initiate legal proceedings (Davies, 2002: 251; Parkinson, 1993: 241-245; Reisberg, 2007: 84-87; Siems, 2008: 211).

Regarding the first of these, it is plain that the minority shareholders’ ability to seek redress under Part XI JSCA is predicated on detecting instances of misappropriation and obtaining sufficient documents to evaluate the merits of embarking upon litigation and to prepare to issue a claim (Parkinson, 1993: 243, 244; Reisberg, 2007: 85, 86). Article 125 of the APC 2002, as is likely with civil procedure rules elsewhere in the world, requires claimants to state their complaints by reference to specific legal provisions and to identify the circumstances

that gave rise to the complaints.³ A shareholder claimant would therefore have to identify a transaction, and a section 81 JSCA conflict of interest therein, that was completed in the absence of the requisite Part XI approval in the particulars of claim.

The information necessary for this purpose should in principle come from the mandatory disclosure of related party transactions.⁴ The difficulty here, however, resides with ensuring that the disclosure obligations are observed because *ad hoc*, as opposing to periodic, disclosure obligations are notoriously difficult to enforce. If disclosure is not anticipated, it is difficult to know when the obligations have not been complied with. Thus, regarding the *ad hoc* disclosure, it has been authoritatively observed that ‘vigorous legal enforcement alone seems to be able to ensure compliance’ (Kraakman et al, 2009: 50). However, as was explained in Chapter 2, the Russian disclosure provisions do not appear to provide the necessary sanction to incentivize controllers to disclose related party transactions. For this reason, it is fair to assume that the information that would be needed to file claims under Part XI JSCA is unlikely to surface pursuant to the mandatory disclosure obligations.

Certainly some relevant information may be brought to shareholders’ attention from other sources. For example, annual profit and loss and balance sheet figures may be sufficient to give rise to suspicion. Shareholders may be able to infer overreaching from changes in the annually reported financial outcomes (Cooter and Freedman, 1991: 1049; Parkinson, 1993: 243). Shareholders may also become aware of wrongdoing through press speculation or from whistleblowers (Reisberg, 2007: 87). Indeed, the available empirical evidence concerning the information available to participants in Russian financial markets alluded to in Chapter 2 indicates that minority shareholders ‘are not completely in the dark’ (Chernykh, 2008: 186). And perhaps there will be occasions where such anecdotal sources would produce more specific evidence of transactions and conflicts sufficient to put together the initial pleadings for the purposes of article 125 APC 2002 and thereby engage the APC interlocutory disclosure provisions on the basis of which further evidence could be sought.⁵

But it is reasonable to suggest that such instances are more likely to be sporadic than regular. For the detection of, and the gathering of evidence on, misappropriation by minority shareholders to begin to approach systematic levels access to internal corporate books and

³ Article 102 of the 1995 Arbitrazh Procedure Code.

⁴ Chapter 2 p.p. 43 – 47.

⁵ For an overview of the APC discovery process see Oda, 2007: 459-466; Treushnikov, 2005: 212-280.

records would be necessary (Reisberg, 2007: 86). However, as discussed in more detail in Chapter 5, the JSCA only entitles 25 per cent shareholders to access such information. Doubtless, this level of shareholding would preclude the vast majority of aspiring minority litigants from gaining access to the facts that could form the basis of their claim.

Finally, it is also worth noting that the limited minority shareholder access to the necessary data to support optimal enforcement is not unique to Russia (Reisberg, 2007: 86). Indeed, as was discussed in Chapter 2, the information asymmetry is at the heart of the general ‘deterrence deficit’ argument which favours related party transaction rules that remove hurdles to minority actions in order to increase the probability of enforcement by, for example, presuming misappropriation from its appearance (Cooter and Freedman, 1991: 1053, 1054). As such the information asymmetry features prominently in the welfare maximisation analysis of the procedural rules carried out in Chapter 5 where it will be argued that the efficient rules should (i) vary to reflect the claimants’ access to internal corporate records under the JSCA; and (ii) incentivize the disclosure of information on conflicts and transactions to shareholders.

The second reason why minority shareholders may not pursue claims under Part XI JSCA that have a net present value for all the expropriated minority shareholders of a company concerns the insufficient incentives to initiate legal proceedings. Any recovery from a successful Part XI claim, be it compensation or restitution, will accrue to the company and not exclusively to the minority claimant. Hence, such claimants would expend effort and incur costs in investigating and pursuing the action but would only benefit to the extent of their shareholding. It is conceivable that if the costs of pursuing the claim are considerable this alone would act as a strong disincentive to bringing the action. And jurisdictions with high direct litigation costs often respond to this problem by amending their ordinary costs rules to permit shareholders to recoup their costs from the company or by allowing some sharing of the costs and benefits of the action between shareholders and their legal representatives (Kershaw, 2009: 568-576; Reisberg, 2007: Chs. 6 and 7).

The funding of claims brought by shareholders on behalf of companies is an enormous topic in itself.⁶ Its proper exploration is beyond this thesis. For the present purposes suffice it to note that the direct costs of bringing a claim in Russia are ‘negligible’ (Hendley, 2004: 319,

⁶ For an overview see Reisberg, 2007: Chs. 6 and 7.

327-330). In fact the low costs are often criticised as failing to filter out meritless litigation rather than as providing a disincentive to file claims (Dobrovolskii, 2007: 341).

Thus, the APC requires claimants to pay an up-front filing fee ('gosposhlina') based on a percentage of the amount sought specified in the RF tax legislation.⁷ Yet the amounts are capped at very low levels. For compensation claims the fees cannot exceed RUB 200,000 (approximately GBP 4000 at the time of writing) and for claims seeking to rescind a transaction the flat fee is RUB 4000 (GBP 80).⁸ Moreover, the fee can be deferred to the conclusion of the case and, as the empirical data suggests, most of the applications for the deferment are granted (Hendley, 2004: 328).

The APC adopts the 'costs in the case' rule meaning that the loser bears the winners litigation costs, which include the up-front fees, expenditure on witnesses and experts and the reasonable costs of legal representation.⁹ Undoubtedly the rule can provide a significant disincentive to minority shareholder claims (Kershaw, 2009: 570) and the empirical evidence on how arbitrazh courts have approached the rule appears to be lacking. However, the 'enormous' caseload in arbitrazh courts with the majority of claimants pursuing 'paltry' sums is a strong indication to the contrary (Hendley, 2004: 317, 318; Oda, 2007: 456). The direct litigation costs do not appear to obstruct legal actions in Russia generally, and there is no reason to believe that the position might be different regarding shareholder actions specifically.

More fundamentally, even if the direct litigation costs are negligible, or are overcome by means of special costs provisions, this in itself does not provide shareholders with a positive incentive to sue (Davies, 2002: 251; Parkinson, 1993: 241; Reisberg, 2007: 88). The reason for this is based on the fact that shareholder actions to redress controllers' wrongdoing have a characteristic associated with commodities that economists describe as public goods namely, nonexcludability – the inability to exclude non-paying beneficiaries from consuming the commodity (Cooter and Ulen, 2004: 46, 47; Whincop, 2001: 123). An aspiring minority claimant would still have to expend a considerable effort on monitoring and investigating misappropriation whereas the benefit of the effort will be shared with other shareholders, who will not have incurred any of the costs. This creates the incentive for minority shareholders to 'free-ride' on the back of the efforts of others – to hang back, hoping that

⁷ Article 102 APC.

⁸ Article 333.21.1.(1) and (2) of the RF Tax Code 1998.

⁹ Articles 101, 106, 110 APC.

another will step in – with the ultimate consequence that no one steps forward to address the problem.

This is one aspect of what is known as the shareholder collective action problem – it is rational for minority shareholders to remain apathetic (Cheffins, 1997: 140-141; Davies, 2002: 139, 140; Posner, 1998a: 441; Easterbrook and Fischel, 1991: 66, 77, 78). Economic scholarship posits that due to the nonexcludability too little public goods will be produced if their provision is left to private actors (Cooter and Ulen, 2004: 47; Scott, 2003: 428, 429). In the same vein too little enforcement under Part XI JSCA is likely to take place if left to minority shareholders.

In sum, minority shareholders may not have the incentives to act as potent enforcement agents under Part XI JSCA even if provided with an unfettered enforcement right. Certainly, the incentives problem is not a positive reason to curtail minority shareholder enforcement. The problems set out in the following section are. But it does suggest that the minority litigation should not be seen as the panacea against controllers' overreaching.

At the same time, caution is necessary in lumbering all minority shareholders under one umbrella. Not all shareholders are likely to suffer from the collective action problem to the same extent. It is conceivable that some minority shareholders will have sufficient shareholding to justify the expenditure of resources on monitoring and challenging suspect related party transactions. The absolute value of a shareholder's investment in the firm may result in the net gains for the shareholder and thus justify the costs of intervention even if other minority shareholders will be able to free ride on the shareholder's effort (Parkinson, 1993: 166-168, 242).

To be sure the effective enforcement by substantial shareholders cannot be presumed and some Russian studies have suggested that the investors with large enough stakes may opt to collude with insiders rather than champion the interests of the minority (Dolgopyatova, 2004: 50). Yet, the above discussion of the collective action problem suggests that the most promising bulwark against the minority shareholder expropriation is likely to be in the hands of the substantial shareholders.

4.1.2 Improper enforcement problems

As to the positive reasons to curtail minority litigation, it is helpful to begin with an observation that not every actionable infringement of Part XI JSCA should be pursued through the courts. First, as was explained in Chapter 2, because of the direct costs of obtaining approval under Part XI and the indirect costs associated with strategic voting it is conceivable that some related party transactions would be executed without the requisite approval. For this reason the absence of the approval should not entail overreaching in every instance. Some unapproved related party transactions would be beneficial to the company and its minority shareholders and should not, in principle, be rescinded.

Second, the pursuit of even well-founded actions is not always in the interests of the company and the expropriated minority shareholders. The overall costs of the litigation in terms of lost management time, adverse publicity and the effect on the, continuing, relationship with controlling shareholders may outweigh any gains to minority shareholders from rescinding expropriatory transactions (Parkinson, 1993: 245, 246; Davies, 2008: 605, 606). Finally, even those actions that accrue net gains to minority shareholders as a group may result in welfare losses to society and therefore should not be pursued on this basis. These are the actions that adversely affect the interests of third parties who enter into transactions without notice of the Part XI violations (Fox, 1998: 493; Worthington, 2003: 89).

Of course it does not automatically follow from the above that the shareholders would pursue every Part XI infringement through the courts. *Prima facie* bringing suits destructive of shareholder value is irrational for, as Reisberg points out, ‘if the company prospers then, generally speaking, the shareholders will also prosper’ (Reisberg, 2007: 85). Shareholders’ investment in a company should make them sensitive to the effects of their actions on the company’s value. In principle therefore, one might expect the shareholders to pursue only those actions that result in net gains to the company and the minority as a group, even if not in the net social benefit.

However, collectively irrational behaviour could still be rational from the perspective of an individual shareholder. Thus, in the preceding section it was explained how the collective action problem dampens shareholders incentive to seek judicial redress against expropriation. There is an additional aspect to the collective action problem that incentivises the individual

shareholders to litigate when it may not be in the interest of minority shareholders as a whole to do so.

This aspect of the collective action problem has two facets. On the one hand, minority litigants do not bear the full costs of litigation but only the fraction commensurate with their shareholding, which may be negligible. On the other hand, they may seek to obtain a collateral benefit not shared with others from the litigation (Davies, 2008: 609). It is foreseeable that the conflicts of interest and the holdup problems discussed in Chapter 2 that lead some shareholders to strategically vote against transactions equally arise in the enforcement context except that perhaps more acutely given the absence of the ‘majority of the minority’ approval requirement to commence legal action. In the extreme, but not unheard of in Russia (Telukina, 2005: 582) a competitor may acquire a share in the company with the sole purpose of pursuing malicious litigation.

More generally, shareholders with small stakes have strong incentives to bring suits against companies even where the prospect of prevailing before a court is small so long as the cost of filing the claim is less than the defendant’s cost of putting up the defence. Such nuisance, or strike, suits are brought for their settlement value and only benefit claimants, and their legal representatives, but leave the companies worse off.¹⁰ Thus, in the United States, where the ability of individual shareholders to bring suits is considered to be relatively uninhibited in comparison to other jurisdictions,¹¹ commentators have noted the prevalence of settlements in the shareholder derivative litigation despite the reported judgments tending to favour defendants by ‘an overwhelming ratio’ (Coffee, 1985: 9). The disproportionate ratio between the claimant and the defendant victories in the US ‘has long been seen as evidence that such actions are typically ‘strike suits’ brought to extort a payment from the corporate treasury’ (Coffee, 1985: 9).

To conclude, it is difficult to summarise the problems with the minority shareholder enforcement more succinctly than Whincop did when he stated that ‘[the shareholders’] unwillingness to create public goods is matched by the willingness to engage in behaviour, the costs of which are primarily borne by other shareholders. A shareholder litigating against

¹⁰ Coffee, 1985; Davis, 1985: 50; Easterbrook and Fischel, 1991: 101; Romano, 1991; Rosenberg and Shavell, 1985. The regulation of settlements was introduced in Russia in 2009: article 225.5 APC now requires courts to withhold their approval of a settlement if it is not in the interest of the company.

¹¹ Principally, but not exclusively, due to the absence of the minimum ownership requirements (Kraakman et al, 2009: 174-176; Parkinson, 1993: 241, 242).

the firm may do so expecting to receive some form of collateral benefit. Because the plaintiff bears only a very small share of the costs the corporation bears, the incentive to abjure such litigation is weak' (Whincop, 2001: 123).

In setting out the difficulties associated with minority shareholder enforcement of related party transactions rules the above discussion provided the necessary background to consider the RF legislature's and courts' responses to the question of the shareholders' *locus standi* under Part XI JSCA. It is to these responses that the discussion will now turn.

4.2 Shareholder *locus standi* under Part XI JSCA

4.2.1 Law

It is helpful to begin the discussion of shareholder standing under Part XI JSCA with an outline of the relevant provisions as at the time of writing the thesis. At present the provisions are fairly elaborate: section 84(1) JSCA expressly sets out who can bring a suit under the section and in what circumstances courts can allow the suit to proceed.

Thus, the section states that '*a transaction in the completion of which there is a conflict of interest, and which is completed in contravention of the requirements set out in the present Federal Act, may be held invalid upon a suit by the company or its shareholder*'. Shareholder *locus standi* is therefore enshrined in the corporate legislation.

Furthermore, section 84(1.3) specifies four conditions the existence of any one of which would require the court '*to decline to invalidate transactions*'. The four conditions are effectively the 'control mechanisms' that are intended, at least *prima facie*, to ensure that actions brought under section 84(1) benefit companies. For the purposes of the present Chapter the conditions can be dealt with in summary.

From the perspective of a shareholder's ability to seek redress under Part XI JSCA the first condition is arguably the most onerous. Pursuant to paragraph 1 of subsection 1.3 the court must dismiss suits brought by shareholders who hold insufficient stakes to have determined the outcome of the vote had the related party transaction been put before the general meeting for the Part XI compliant approval. Self-evidently the provision is designed to 'collectivise' shareholder suits in order to curb the ability of shareholders with small stakes in a company to bring actions. As explained above, legal actions by such shareholders carry the risk of

being contrary to the interests of the company and its shareholder body as a whole. Albeit that the precise shareholding that claimants would need to demonstrate in a given action would doubtless vary with the company and conflict specific circumstances, it is foreseeable that few claimants with a shareholding below say one per cent of a company's share capital would be able to overcome the hurdle imposed by the first condition.

The remaining three conditions are stated in paragraphs 2 to 4 of section 84(1.3). The conditions require the courts to decline the rescission (i) in the absence of actual or potential losses to the company or the claimant shareholder or of other adverse consequences from the transaction; (ii) where an *ex post facto* approval of the transaction was obtained in compliance with the Part XI JSCA requirements prior to trial; and (iii) in the absence of the actual and constructive knowledge of the infringement of Part XI JSCA on the part of the counterparty to the transaction. Disregarding the merits of the four conditions at this stage, it is necessary to point out that they were only introduced into the JSCA in July 2009 by the Federal Act No.205-FZ. Throughout the period surveyed in this thesis the JSCA contained no analogous mechanism to control shareholder litigation under Part XI JSCA.

Furthermore, the shareholder standing was only put on the express legislative footing in August 2001 by the JSCA amendments that took effect in January 2002.¹² There does not appear to be an explicit record why this was so and a number of *ex post facto* rationalisations are possible. For example, it may have been unnecessary to expressly identify shareholders in section 84 in order to give effect to their right to bring claims under Part XI JSCA. As was discussed in Chapter 3, the express standing provision would only have been necessary if the related party transactions were characterised as voidable under the Civil Code. For void transactions this would not have been necessary since, pursuant to article 166(2.2) of the Civil Code, '*any interested person*' – the term of sufficient breadth to encompass individual shareholders – can petition a court to rescind void transactions. At the time of the JSCA's promulgation it may have been assumed that transactions within the scope of Part XI JSCA were void for the purposes of the Civil Code and shareholder standing was, therefore, also assumed as a given.¹³

¹² Federal Law No.120-FZ of 7.08.2001.

¹³ The shift to the voidable characterisation of related party transactions in 2000 would then explain the August 2001 amendment of section 84: the voidable characterisation necessitated express designation of shareholders under section 84 to give effect to their enforcement right.

Alternatively, the omission of shareholder standing could simply have been overlooked. As was also noted in Chapter 3, when judges Novoselov and Mametov suggested that Part XI transactions were voidable in the December 2000 *Vestnik*, they argued precisely that the absence of the shareholder *locus standi* was a legislative oversight rather than the indication of the legislative intention to categorise the transactions as void or to preclude shareholder enforcement (Novoselov and Mametov, 2000: 85). In short, it is possible that the absence of shareholder standing in section 84 was not an intentional design to exclude minority shareholder enforcement of Part XI.

And perhaps the absence of a filtering mechanism in the JSCA may be similarly explained as a legislative oversight. It may also have been deliberately excluded. This is not implausible given the general concern of the post-soviet reformers to establish a capital market economy in Russia and to attract foreign capital into the country by *inter alia* creating a legal environment affable to the world's investing class. The curtailment of minority shareholder enforcement under Part XI JSCA would have been incongruent with this objective.

Yet it is more likely, given the concerns with unfettered shareholder standing discussed in section 4.1, that the omission was intentional which would also account for the absence of a filter to shareholder actions. Notably, the JSCA drafters were alive to these concerns and reflected them in their proposals. Unhelpfully the drafters did not explicitly opine on whether shareholders should have the right to seek rescission of related party transactions under section 84(1), the only provision to feature in the cases surveyed in this thesis. However, as shown below, the genesis of their recommendations suggests that they would have opposed it.

Thus, the drafters thought that section 84(1) was overbroad and could jeopardise the interests of third parties transacting with companies. They suggested that the Part XI requirements should be treated as part of the company's internal governance with the rescission automatically applicable only in respect of transactions concluded with the conflicted persons directly; their close relatives; and with the companies wholly owned by the insiders. In all other cases the drafters proposed that the remedy should only be available if the counterparty 'knew or should have known of the violation of the conflict-of-interest rules' (Black, Kraakman and Tarassova, 1998: 461). Given their disapproval of the remedy, it is unlikely they would have supported unrestrained shareholder recourse to the section, if any.

Their proposal for the enforcement of section 84(2), the compensation provision for losses resulting from Part XI infringements, further supports this suggestion. The drafters stated that shareholders should be able to enforce this section, however, only subject to the one percent shareholding constraint to prevent nuisance suits (Black, Kraakman and Tarassova, 1998: 462). It is near certain their final proposal did not provide for the shareholder enforcement under section 84(1) because they intended it to be excluded. Should it have been otherwise, they would have sought to include the same one percent constraint as in section 84(2), the remedy they thought to be less draconian.

To the extent legislative intent can be inferred from the drafters' proposal, it would support no recourse to section 84(1) by shareholders. And it is likely that the drafters' intent was congruent with that of the legislature: the latter adopted elaborate enforcement right provisions elsewhere in the JSCA according to the drafters' proposals.

The most notable provision in this regard was section 49(8) which empowered individual shareholders to appeal decisions taken by the general meeting in contravention of the JSCA requirements, other RF legislation or the company's charter.¹⁴ Under the section the court had the right, taking into account all the circumstances of the case, to leave the decision in force if the shareholder's vote could not have influenced the voting result, the contravention was not material and the decision did not cause losses to the shareholder. Plainly there would have been an anomaly if the legislature also intended the individual shareholders to bring rescission claims under section 84(1), or at least to bring such claims on more lenient terms than those contained in section 49(8): the shareholders would have been able to contest the validity of a related party transaction before the court in the circumstances where they could not contest the resolution adopting that transaction.

On balance therefore it is a fair speculation that the shareholder standing was deliberately excluded from the original Part XI JSCA. If this indeed was the case, and ultimately there is no sure answer, then arguably the legislature went too far. The arguments set out in section 4.1 go as far as to require a filter to shareholder litigation but not one that would preclude shareholder enforcement in its entirety. Importantly, the absence of the express shareholder

¹⁴ Currently the provision is to be found in section 49(7) JSCA. See also section 71(5), which allows shareholders with one per cent shareholding to sue the directors for damages for losses caused to the company as the result of breaches of the fiduciary duty. For an overview of these and other provisions, which explicitly granted shareholders rights to sue see Black, Kraakman and Tarassova, 1998: 318-320.

standing prior to the August 2001 reforms need not have precluded the courts from granting shareholders standing. As indicated earlier, the Civil Code left scope for the courts to read the standing into section 84. Perhaps a more appropriate characterisation of the events is that the legislature left the difficult task of deciding whether the right to enforce the Part was to be confined to actions brought by companies alone or whether the right also extended to shareholders to the judicial discretion.

Before turning to consider how the FAC approached the task two occurrences that took place following the enactment of the *locus standi* and that are broadly relevant to the thesis's enquiry are worth mentioning. First, the coming into force of the express shareholder standing in January 2002 was followed by a noticeable increase in shareholder litigation under Part XI JSCA. Particularly in 2003 the shareholder claims adjudicated by the FAC increased by 175 percent when compared with the number of such claims in 2002.¹⁵ It is likely that the rise in the Part XI claims was independent of the general increase in litigation before the FAC in that year: the total number of cases appealed to the court only rose by 24 percent and the total number of cases decided by the court rose by 25 percent.¹⁶ The figures suggest that the enactment may have had a significant impact on the shareholders' ability to enforce the provisions of JSCA Part XI.

Second, the reforms were also accompanied by a noticeable rise in the RTS index – the most prominent index of the Russian stock market. Furthermore, according to some commentators, namely Gorjaev and Zabolkin, the August 2001 – January 2002 reforms, i.e. the reforms that have also enacted shareholder standing into Part XI JSCA, played an important role in what they described as 'the most spectacular equity market's re-rating' – the RTS index rallied from 180 to 782 (an increase of 334 percent) between October 2001 and

¹⁵ The number of shareholder claims had risen from eight in 2002 to 22 in 2003.

¹⁶ The figures are based on the statistics disclosed by the FAC on its website <http://fasmo.arbitr.ru:80/fasmo/reports/activity/293.html>. Accessed on 14 July 2010. Due to the webpage no longer being available online a hardcopy of the webpage has been included in Appendix 1 p.p. 13a, 14a.. The average rates of increase between 1999-2003 are 26% for claims appealed to the FAC; and 28% for cases decided by the FAC. These figures offer a useful but an imperfect guide because the FAC does not disclose how the total number of claims is calculated. The easiest way would be to disclose the total number of the court's decisions in that year. However, as was explained in Chapter 1, the figures used in the thesis are accumulated on the basis of the FAC's final judgment: i.e. some cases will involve more than one decision. The method could skew the 175% figure upwards by treating some 2002 decisions as only decided in 2003. In other words, the number of decisions in the previous year could be higher and hence the rate of the increase ought to be lower. This however is not the case. In the sample of judgments in this thesis no FAC judgments in 2003 included the decisions of the court 'carried over' from 2002 - the 175% figure should not incorporate the 'following year' bias.

April 2004 (Goriaev and Zabolkin, 2006: 389). Almost a third of that growth was achieved during the Autumn 2001 – Spring 2002 period: the period covering the enactment and the coming into force of the JSCA reforms.

To be sure, the scale of the reform – some 66 of the Act's 94 sections were amended – renders any inferences of a correlation between the enactment of the express shareholder standing and the RTS index rally at best speculative. And in fairness to Goriaev and Zabolkin, the authors did not go so far as to single out the *locus standi* enactment as the factor behind the stock rally. On the contrary, they thought that the closure of loopholes that allowed controlling shareholders to disenfranchise minorities by means of abusive share dilutions, rather than shareholder standing under Part XI JSCA, was the reform's key achievement.¹⁷ The same is true with respect to other commentators at least to the extent inferences may be drawn from the cursory, or indeed altogether absent, references to the shareholder standing in their analysis of the reform.¹⁸

¹⁷ Goriaev and Zabolkin, 2006: 389. Indeed, Goriaev and Zabolkin identified numerous factors, not related to the legal environment in Russia, that could, at least partially, explain the rise in the RTS index namely, fluctuations in global capital, money and commodity markets (390 – 396); a 'historic compromise' between Putin and Russian business leaders reached during a Kremlin meeting in July 2000 where it was agreed that the private wealth acquired during the 1990s would not be used to interfere with the political system in exchange for a *de facto* amnesty of the 1990s privatisations, strengthening the security of title over the controlling shareholders' assets and thus improving their incentives to increase their firms' market valuation by *inter alia* improving firm-level corporate governance practices; the political stability assured by the parliamentary and presidential elections in December 1999 – March 2000; the macroeconomic stability supported by a recovering price of oil and prudent fiscal policy by mid-2000; the new administration's readiness and ability to pursue serious structural reforms, starting with the introduction of a flat 13 percent income tax and other radical tax reforms; the external shock of 11 September 2001 and its geopolitical consequences whereby Russia emerged as an ally of the US and others in the new 'war against terror' (389).

¹⁸ In the introduction to her commentary dedicated specifically to the 2002 reforms, Shapkina highlights a number of what she thought were the key changes intended to improve the protection of minority shareholders without any reference to the section 84 amendment (Shapkina, 2002: 7). In the section dealing specifically with the amendments to Part XI JSCA, Shapkina merely mentions that the amendment added a specification that the invalidity claims may be brought by companies and shareholders, only emphasising that the transactions remain voidable and that the invalidity claim may be brought not only on the ground of a breach of section 83 but also for a breach of the legislation generally (Shapkina, 2002: 178). Similarly Shitkina's analysis of the 2002 changes points out several shortcomings in the amended Part XI without any mention that the shareholders now had an express *locus standi* enshrined in section 84 (Shitkina, 2002). Other authors simply observe that companies and shareholders can bring invalidity claims under Part XI without mentioning whether the situation might have been different prior to 2002 (eg. Gabov, 2005: 360). Oda, on the other hand, observes that there was a debate concerning whether transactions were void or voidable prior to the reform and that it was settled in favour of the voidable characterisation but which could be invalidated by companies as well as shareholders (Oda, 2007: 181). Telukina, the only author found to make such a statement, states that of the outmost importance was the innovation that specified the subjects who can bring claims under section 84. She states further that at present such subjects were the company or any of

Nevertheless, *prima facie* the pattern of shareholder litigation and the rise in the index suggest that minority shareholders may not have been able to enforce Part XI JSCA prior to the August 2001 reforms coming into force and that perhaps this apparent inability might have arrested the development of the stock market. The litigation pattern and the RTS index appear to support, however speculatively, the JSCA drafters' conclusion that the absence of the institutional infrastructure to control self-dealing by managers and controlling shareholders – 'the essential fertiliser', as they put it – prevented the emergence of Western-style capital markets despite the existence of 'decent laws' in Russia (Black, Kraakman and Tarassova, 2000: 1755, 1756, 1757, 1769, 1782, 1797). The judicial reluctance to grant shareholder standing, if there was any, would arguably undermine the effectiveness of Part XI and to this extent would perhaps offer the strongest evidence yet in support of the arguments that under-enforcement of the rules arrested the progress of Russian equity market.

The ensuing discussion therefore considers three specific questions: (i) did the FAC deny shareholder standing under Part XI JSCA prior to January 2002? (ii) did the FAC impose a requirement in shareholder actions that the claimants cannot satisfy under any circumstances, in effect denying shareholder standing 'via the back door'? The latter question is directed at a specific criticism expressed by certain commentators that Russian arbitrazh courts have developed jurisprudence, which for convenience may be described as the 'rights and interests requirement', that either purposefully or in effect precludes the minority shareholder actions. And if the answers to the first two questions appear negative then, (iii) what explains the rise of shareholder litigation under the Part that followed the enactment of the express *locus standi* for shareholders?

4.2.2 Judicial treatment of shareholders' *locus standi* under Part XI JSCA

Literature on the locus standi prior to the August 2001 reform

Earlier it was suggested that the commentary on the August 2001 JSCA reform made only cursory reference to the section 84 amendment that placed individual shareholder standing on the statutory basis. One would expect the amendment to have been greeted with more fanfare

its shareholders. However it is unclear whether the reference to the present indicates that in the past the situation was different, or whether it is likely to change in the future (as it in fact has in 2009). Also she provides no discussion why that innovation was important (Telukina, 2005: 84).

had it affected the minority shareholders' ability to bring claims under section 84 in a material way. The muted response from the academy suggests that the amendment did not affect the standing materially, that the courts allowed shareholder actions under section 84 despite the absence of the express *locus standi*. However, since other JSCA amendments may have reasonably diverted the commentators' attention positive evidence of shareholder enforcement of Part XI JSCA prior to the reforms would offer a more concrete basis for believing that the courts allowed shareholders to litigate under the Part.

In this regard, certain commentators have stated more affirmatively that 'the courts adhered to the [individual shareholder standing] principle prior [to the reform]', albeit without reference to the decided cases and presumably on the basis of their personal litigation experience (Budylin, 2005: 23). Notably, the available extra-judicial commentary by the Russian judges is of the same view (Faizutdinov, 2001: 7). Thus, in their *Vestnik* article referred to above and in Chapter 2 judges Novoselov and Mametov, although sceptical of the merits of endowing the individual shareholders with standing under section 84, thought that the courts were bound to permit shareholder claims in the absence of the express legislative bar. The two judges were apprehensive of the opportunistic shareholder litigation under Part XI JSCA and its consequences for the stability of the markets for goods and services in Russia. As they put it, it was 'doubtful that providing a practically unrestricted circle of persons with the right to challenge transactions under section 84 will have a positive influence on the civil exchange and on the protection of proprietary rights of a joint stock company' (86).

They recommended that section 84 be amended to expressly state that only companies could bring the section 84 claims. If the legislature deemed it necessary to extend the standing to shareholders the judges suggested that such actions should be restricted to claimants who could amass at least five percent of the company's share capital (87). Crucially however, Novoselov and Mametov concluded that in the absence of a legislative change section 84 had to be interpreted by analogy with section 45(5) of the Limited Liability Companies Act 1998 as permitting individual shareholders to bring actions to invalidate defective related party transactions (87). As will be shown below, the case data bears this out.

However, before turning to the cases one final point raised in the literature that concerns shareholders' standing requires attention. At the heart of the issue is the fact that courts could bar shareholder enforcement of Part XI JSCA, intentionally or inadvertently, without holding

overtly that a shareholder does not have *locus standi* under the Part. It is not difficult to imagine courts imposing a particularly onerous requirement that few shareholders could discharge or a pre-condition to actions that would only arise in exceptional circumstances.¹⁹ The requirement or the pre-condition of this kind would in effect act as a *de facto* bar to shareholder actions and would do so irrespective of whether shareholders' standing is enshrined in legislation. In other words, the point touches on shareholders' standing generally and is not limited to the state of affairs prior to the August 2001 reforms. The suspect jurisprudence in question is what the thesis will call the 'rights and interests requirement', which according to one author has 'in reality become an insurmountable obstacle to challenging the [related party] transactions' (Gudieva, 2007: 47).²⁰ The requirement and its criticism are considered next.

Literature on the rights and interests requirement

There is no mention of the requirement in Part XI JSCA although it does feature elsewhere in the Act. For example, section 49(8) which empowered individual shareholders to appeal certain decisions taken by the general meeting that was alluded to above stated that a shareholder had the right to sue only if his rights and legal interests were violated.²¹ In the context of the related party transactions rules, the requirement was legislatively recognised – with legislation loosely defined for this purpose to include Decrees issued by the SAC – for the first time in November 2003.²² Paragraph 38(2) of the SAC Decree No.19 of 18 November 2003 provided that '*claims brought by shareholders to hold invalid the*

¹⁹ For example, in the UK the pre-Companies Act 2006 wrongdoer in control principle has been criticised for running 'the risk ... of rendering minority actions barely conceivable' in public companies (Parkinson, 1993: 249).

²⁰ She, however, concedes that the practice is not uniform (47). Dobrovolskii, on the other hand, is less critical in the evaluation of such doctrine at least to the extent he states that the courts insist on proof of breach of rights and interests 'without doubting a shareholder's right to challenge a transaction' (2006: 178). However his analysis clearly shows that the *de facto* outcome is the inability to bring such challenges. For example, he states that members of LLC have a greater chance of success since s.s. 15, 26 of the LLC Law 1998 guarantee that the value of the share must reflect real assets which allows the members to argue that transaction affected this value. This he argues is unavailable to shareholders where no such guarantees are given (2006: 179, 180).

²¹ Now section 49(7) JSCA.

²² Para. 38 of the SAC Decree No.19 (18 November 2003) was the first 'quasi-legislative' instrument to expressly enunciate the requirement albeit without specifying the rights and legitimate interests shareholders had, thus, offering no guidance as to what shareholders would need to demonstrate in Part XI JSCA invalidity claims to satisfy this requirement.

transactions completed by joint stock companies may be satisfied in cases where evidence is presented that demonstrates an infringement of rights and legal interests of the shareholder’.

As to the SAC related party transactions jurisprudence, the requirement first surfaced in *Постановление Президиума ВАС РФ от 12.11.02 No.6288/02* almost a year to the day preceding the Decree No.19. The FAC, however, began dismissing shareholder suits brought under Part XI on the ground that the claimants failed to demonstrate a breach of their rights and interests as early as November 2000.²³ The court founded its decisions on the Arbitrazh Procedure Code 1995 (‘the APC 1995’) which in article 4(1) stated that ‘*an interested person has the right to petition an arbitrazh court for the protection of [his/her/its] infringed or disputed rights and legal interests...*’.²⁴ Thus, although paragraph 38(2) is commonly taken to be the legal authority for the requirement (Dobrovolskii, 2006: 173; Gabov, 2005: 360, Shitkina, 2008: 523), its legal origin is in the APC 1995. Indeed, this much was acknowledged in the preamble to paragraph 38(2), paragraph 38(1), which provided that the courts had to consider shareholder suits ‘*in accordance with APC RF*’.

Of more practical importance to this thesis is the fact that for some time the FAC was developing the requirement’s content in its Part XI adjudication without express sanction or guidance from the legislature or the SAC. Furthermore, the substantive content of the requirement remained unsettled by a higher order legal authority throughout the period surveyed in this thesis. Although the SAC Decree No.19 explicitly sanctioned judicial recourse to the requirement in November 2003 it did not specify what shareholder claimants would have to demonstrate to discharge the requirement.

More guidance was provided by the earlier *Постановление Президиума ВАС РФ от 12.11.02 No.6288/02* in that the court held that the evidence of damage from the disputed transaction was a *necessary* factor in establishing that the claimant’s rights and interests were infringed. However, at no point in its judgment did the SAC state that the proof of losses was *sufficient* to discharge the requirement. The question remained unresolved until the SAC Decree No.40 of 20 June 2007 which provided that an infringement of the claimant’s rights and interests is to be presumed where the court establishes that the transaction caused losses

²³ *Постановление ФАС Московского округа от 09.11.00 по делу N. КГ-А40/5072-00* CDN44 was the first case in the case data to raise the issue.

²⁴ The Arbitrazh Procedure Code 2002 (the ‘APC 2002’), which replaced the 1995 Code, retains this provision, which has also largely survived subsequent amendments to the 2002 Code.

to the company, unless the contrary is proved.²⁵ Albeit the Decree, in referring to the proof to the contrary, left open the possibility that there may be circumstances that could prevent the invalidity even where the transaction causes losses to the company, its central emphasis is on the damage to the company and, therefore, the possibility to refuse the invalidity remedy in such circumstances is considered ‘more likely theoretical’ (Eremenko, 2007: 52).²⁶

The uncertainty over the requirement’s substance was also reflected in the academic commentary, which, as shown below, did not provide an unequivocal answer. Much of the discussion during the period preceding the SAC Decree No.40 was polarised over the question whether the noncompliance with Part XI JSCA was sufficient to invalidate a related party transaction, or whether it was also necessary to demonstrate that the company has incurred losses.²⁷ As a result of this polarisation an important construction of the rule, which, if adhered to by the courts, could be detrimental to the shareholders’ ability to bring the section 84 invalidity claims was overlooked. Because commentators, with few exceptions, coalesced around the question of whether the proof of losses was necessary, they missed the point that the proof of losses might have been insufficient.

It is submitted that the uncertainty is rooted in a deeper ambiguity over the jurisprudential ontology of the shareholder suit under section 84 to rescind a defective related party transaction. Specifically it is unclear, and remains so at the time of writing, how the suit is to be characterised namely, as a special statutory mechanism for the enforcement of Part XI JSCA; as a derivative action brought to redress wrongs committed against the company; or as a direct action brought to redress infringements of the shareholders’ personal rights and the harm caused to the shareholders’ in their individual capacities. Thus, the discussion of the characterisation of the suit is a helpful starting point to understanding the requirement’s possible permutations and, in particular, the permutation that could result in the shareholders being *de facto* barred from bringing actions under Part XI JSCA.

As to the ontology of the section 84 suit, the common law countries’ jurisprudence on derivative actions offers a useful contrast having been credited with the action’s invention

²⁵ Para.3. The Decree stated further that the burden of proving the absence of losses rested with the defendant.

²⁶ See also Shapkina, 2009: 187; Jarkov, 2007: 54.

²⁷ Black et al, 2006b make no reference to the rights and interests, stating only that losses is one of the questions left open by the legislation (English version: 53).

and having benefited from over 150 years of the relevant case law (Clark, 1986: 639).²⁸ Broadly speaking, albeit with the risk of oversimplifying what is indeed a very rich jurisprudence, the common law jurisdictions treat infringements of conflict of interest rules, such as the rules contained in Part XI JSCA, as wrongs committed against the company rather than its individual shareholders. It follows that in such cases the ‘proper plaintiff’, claimant in modern legal parlance, is the company (Kershaw, 2009: 534). However, in recognition that the company may be unable to enforce these infringements because it may be under the control of the people who have perpetrated the wrongs, the common law courts have developed exceptions to the rule.²⁹

An in depth exploration of the exceptions is beyond the scope of this thesis. The more important exception for the present purposes is the derivative action. It allows shareholders to bring suits to redress the wrongs committed against the company provided certain conditions are met, the principal of which is that the wrongdoers in one way or another control the company. Thus, historically the derivative suit was conceived as ‘two suits in one’: (i) a suit against the company seeking an order compelling it (ii) to bring a suit for relief against some third person who had caused legal injury to the company (Clark, 1986: 639). The company would feature as the defendant in the action but only nominally, ‘put into that position because it must be a party to the proceedings but cannot be a plaintiff’ (Rajak, 1995: 534).

This is not to say that common law jurisdictions have faced no difficulties in characterising shareholder claims seeking redress under related party transaction rules. They clearly have, not least since an aberrant conduct, for example voting by a conflicted party to approve the deal, could cause both the corporate injury and the infringement of the individual shareholder’s voting rights and to a large extent it is up to the shareholders to decide whether to formulate their claims as direct or derivative actions. Nevertheless, the conceptual default position remains that the infringements of related party transactions rules are the wrongs against the company and as such their redress is in the hands of the company with shareholders, in effect, bearing the residual enforcement right confined to the circumstances where the company is unable to sue. Apart from the doctrinal logical consistency, the

²⁸ See also Whincop, 2001 describing *Foss v. Harbottle* (1843) 67 ER 189, a leading English authority on the derivative suit, as the Old Testament of corporate law (139).

²⁹ See *Burland v. Earle* [1902] AC 83 explaining the derivative suit exception as instantiating judicial desire ‘to give a remedy for a wrong which would otherwise escape redress’ per Lord Davey at 93 (Reisberg, 2007: 92).

common law ‘proper plaintiff’ and the ‘wrongdoer control’ principles that underpin derivative actions provide an avenue against opportunistic litigation in that if a company can in principle bring a claim, i.e. it is not under the wrongdoers’ control, then shareholders will be precluded from doing so (Clark, 1986: Ch. 15; Kershaw, 2009: Ch. 15).

In Russia such jurisprudential questions are yet to be worked out. Notably, the concept ‘derivative action’ is not expressly addressed by legislation in Russia.³⁰ Nevertheless, the topic has generated a substantial body of literature there. The literature is primarily concerned with resolving the issues the suit poses for the arbitrazh court procedure, for example the status of a company for whose benefit the suit is brought as a claimant, respondent or a third party,³¹ and, to this extent, it has little bearing on the issue of what the rights and legitimate interests requirement obliges claimants to demonstrate.

However, it also discusses the nature of the section 84 invalidity suits brought by shareholders, and whether such suits ought to be categorised as derivative.³² The discussion has proceeded in parallel, and sometimes without explicit reference, to the commentary on the rights and legal interests requirement. Therefore, the following analysis attempts to reconcile the two bodies of literature only in so far as it furthers the understanding of the possible interpretations of the rights and interests requirement. It does not seek to reconcile all the arguments into a coherent whole.

Thus, the first view of what the rights and interest requirement entails argues that the shareholder claimants have to show some evidence that harm was caused to the company from the challenged transaction before a court could grant the rescission. For ease of reference, the thesis will refer to this view as the ‘economic harm approach’. The view is the most congruent with the literature that treats the section 84 claims brought by shareholders as derivative.³³ To be sure as a matter of logic it need not automatically entail that simply

³⁰ In Russia the term is defined as *kosvennyi* or *proizvodnyj isk* – indirect claim. In 2006 the SAC considered introducing an Information Letter that would expressly address the issue but felt unable to do so for fear of encroaching on the RF legislature’s powers (Jarkov, 2007: 53; Gureev, 2007: 145).

³¹ The full breadth of the issues is beyond the scope of this thesis. It is sufficient to note that Part 28.1 introduced into the APC 2002 in 2009 has addressed some of the issues to varying degree of success. For an analysis of the proposals as the provisions then were see Rozhkova, 2007.

³² The two types of claims that the commentators agree are ‘derivative’ despite the absence of an express legislative measure characterising them as such are (1) art. 53 Civil Code and s. 71 JSCA claims against management organs for losses caused to the company; and (2) art.105 Civil Code and s.6 JSCA claim against parent company for losses caused to subsidiary. See Gureev, 2007: 143, 144; Shapkina, 2009: 177; Gros and Dedov, 2007: 157; Rozhkova, 2007: 30.

³³ Shestakova, 2008: 103-106; Gureev, 2007: 143, 144; Jarkov, 2007: 54, 55; Shapkina, 2009: 187.

because a shareholder brings the claim on behalf of the company proof of losses should be necessary. However, on the one hand, some Russian adherents of the view take precisely the stance that the one follows the other: since the shareholder's interest in holding the transaction invalid is indirect – a *de facto* devaluation of the economic value of the shareholding as opposing to an infringement of a *de jure* entitlement – the shareholders will be required to demonstrate that the transaction had some adverse consequences for the company (Shestakova, 2008: 106; Shapkina, 2009: 183).

On the other hand, the implication from the derivative action characterisation is not only that the proof of loss may be required but also, and more importantly, that once the transaction is established to be loss-making, no further proof of effects on shareholders' rights is necessary (Shapkina, 2009: 187; Jarkov, 2007: 54). Since the suit is to enforce the rights vested in the company the effects of the transaction on a shareholder's rights is an irrelevant consideration to the question of whether the shareholder can issue proceedings. Put short, on this view the proof of loss is both the necessary and sufficient condition to discharge the rights and interests requirement.

The second, 'strict approach', view posits that the section 84 shareholder suit is a special statutory mechanism for the enforcement of Part XI JSCA, which expressly grants the enforcement right to shareholders (Rozhkova, 2007: 35; Gros and Dedov, 2007: 158). Congruent with this analysis is the literature which maintains that the shareholders' right to seek the rescission is unconnected to an infringement of their rights and legal interests:³⁴ in stating that the infringement had or had not occurred, the courts are merely restating that a breach of Part XI JSCA had, or had not occurred. On this view the requirement imposes no additional substantive obligation on shareholders over and above having to establish that a Part XI JSCA provision has been breached – the proof of losses, or other effects on shareholders, is not necessary.³⁵

³⁴ Indeed Gros and Dedov state that the shareholder s.84 claims are unproblematic. They suggest that theoretically there might be a difficulty in enforcing the court's restitution order since under the general rule the claimant can compel the other party to obey the order for his benefit, but in s.84 claims the compulsion would be for the benefit of the defendant. However, as the authors themselves state, such original construction has not occurred in practice. Such problems, they state, only occur when the claimant shareholders try to enforce damages order for the benefit of the company. This problem has now been addressed in article 225.8(1) APC 2002 as amended in July 2009.

³⁵ See Shitkina, 2008: 522, 523. It is also worth pointing out that Shitkina opined that, in order to prevent abuse of law and to ensure the stability of the economic exchange, such a requirement should be imposed on shareholders. Shitkina, however, provides no explanation as to what this would entail

Finally, the third, ‘*de facto bar*’, view suggests that the courts treat the shareholder suits as direct actions brought to enforce their personal rights. Since shareholders have no legal entitlement to receive dividends and no legal title to the company’s assets, with the restitution effected between the parties to the transaction and thus leaving the shareholders’ legal rights unaffected (Dobrovolskii, 2006: 179),³⁶ on the basis of this interpretation, even where a transaction is shown to have caused losses, the shareholders will be unable to demonstrate to courts that this amounts to an infringement of their rights and legitimate interests. Such an interpretation of the law, it is argued, undoubtedly correctly, is tantamount to a denial of shareholder *locus standi* in the section 84 invalidity claims.

Whether, and to what extent, the FAC jurisprudence reflects the *de facto bar* interpretation is considered in the next section alongside the remaining two questions posed above namely, whether the FAC denied shareholder standing under Part XI JSCA prior to January 2002 and what explains the rise of shareholder litigation under the Part that followed the enactment of express *locus standi* for shareholders?

4.2.3 Case data

As to the pre-reform shareholder standing, the analysis of the case data is straight forward. Between 1999 and 2001 the FAC examined nine shareholder claims involving Part XI JSCA. In seven cases the court declined to invalidate transactions. In 2002 the court examined eight shareholder claims, declining the invalidity in seven cases. Eleven out of the 14 unsuccessful claims were dismissed on the substantive grounds. The remaining three cases were decided on the following procedural grounds: the contemporaneous ownership rule;³⁷ the breach of rights and interests requirement;³⁸ and the statute of limitations.³⁹ None of the claims brought by the shareholders were dismissed on the ground that shareholders lacked *locus standi* under

in practice. See also Eremenko, 2007 commenting that prior to the 2007 Decree all these considerations were extraneous to the judicial decision as to whether transaction should be invalid (52). Similarly, Telukina, 2005 in her discussion of s.84(1) notes that there are no additional requirements that a shareholder would need to demonstrate beyond that Part XI process has been breached (582). It is also important to point out that she does not support the view.

³⁶ An analysis of shareholders’ personal rights under the JSCA and the Civil Code is beyond the scope of this thesis. For a comprehensive review of such rights see Shitkina, 2008: 387 – 411.

³⁷ Постановление ФАС Московского округа от 2.10.01 по делу N. КГ-А40/5398-01 CDN53.

³⁸ Постановление ФАС Московского округа от 9.11.00 по делу N. КГ-А40/5072-00, Постановление ФАС Московского округа от 5.06.01 по делу N. КГ-А40/2619-01 CDN44.

³⁹ Постановление ФАС Московского округа от 30.05.02 по делу N. КГ-А40/3309-02 CDN67.

Part XI JSCA. The court does not appear to have used the absence of the express standing provision to preclude shareholder enforcement.

This is further supported by the judgments that expressly and positively confirmed that shareholders had standing under the Part. The most important judgment is *Постановление ФАК Московского округа от 19.05.99 по делу N. КГ-А40/1396-99* CDN5. The judgment is important for two reasons. First, it is the first section 84 claim brought by a shareholder to be examined by the court within the case data. Second, the judgment characterised the challenged transaction, an issue of shares, as voidable. The judgment therefore offers an insight into whether the shift to voidable characterisation was intended to curb shareholders' recourse to section 84.

The claim was dismissed both at the first and appellate instances for lack of standing and on other grounds. In particular, the two lower courts held that in accordance with article 166(2) of the RF Civil Code claims to rescind voidable transactions could only be brought by the persons specified in the Code. And since neither the Code nor section 84 specified shareholders, the claimant lacked standing to seek to rescind the transaction. The FAC upheld the two decisions but only in part. It dismissed the claim on the ground that the transaction received the Part XI compliant approval *ex post facto* and was therefore valid.⁴⁰ On the question of standing, however, the court held that the lower instances erred in their interpretation of the law. In doing so the FAC offered the clearest statement that the shift to voidable characterisation should not curtail shareholders' *locus standi* under Part XI JSCA. The court held as follows:

'In fact section 84 of the Law on the Joint Stock Companies does not establish the circle of persons who may file a claim to hold a transaction invalid. However, according to the meaning of the said section such a claim may be filed by an injured person, whom it is necessary to recognise as the company itself as well as the individual shareholders. Accordingly, it is necessary to find the conclusion of the [lower instance] court that an inappropriate person filed the claim as wrong.'

⁴⁰ This is perhaps the reason for the court to characterise the transaction as voidable since it might more difficult to maintain that transactions void *ab initio* can be approved *ex post*.

In two of the three successful shareholder claims it appears from the FAC judgments that the question of shareholder standing was not argued at all.⁴¹ In *Постановление ФАК Московского округа от 20.10.99 по делу N. КГ-А40/3359-99* CDN14 the FAC upheld the lower instance courts' judgments, which invalidated the disputed transaction, stating that the courts were correct to establish that the transaction affected the claimant's interests. This suggests that the defendants raised the *locus standi* point but unsuccessfully. Finally, in *Постановление ФАК Московского округа от 06.12.01 по делу N. КГ-А40/7132-01* the court dismissed the claim, brought by the defendant company's creditor, for lack of the *locus standi* stating that there were 'no reasons to believe that the section 84 claim may be brought by any persons other than the joint stock company itself or by its shareholder'.

In sum, the FAC jurisprudence prior to the JSCA amendment to expressly provide for the shareholders' right to enforce the Act's Part XI demonstrates that the court did not interpret section 84 to explicitly refuse the shareholders' *locus standi*.

As to the rights and interests requirement, the interpretation of case data is more difficult. The FAC has cited the requirement in 34 judgments that dismissed the shareholders' actions. In 28 cases the court relied on other, additional, grounds in its judgment, meaning that the requirement has featured in 6 cases as the sole ground for the dismissal. In these cases it is difficult and probably impossible to establish with certainty what ground was persuasive with the court. Even in the 6 cases where the requirement featured as the sole ground to rule against the claimants there is no certainty that the court relied on the *de facto* bar interpretation or the economic harm approach. Brevity is a general characteristic of the FAC decisions, at least in contrast to the judgments of the common law courts, and even if a judgment is written to suggest that one interpretation was adopted rather than the other it is conceivable that an experienced judge would opt for the least controversial terminology. It is fair to suggest then that there is no sure answer as to what moved the court in a particular case because the judges' true motives are arguably inaccessible. It is possible that it is the additional grounds that influence the court in reaching its decisions. In fact, the adherents of the strict approach would, and do, posit precisely that – on their view the requirement has no independent substantive content (Shapkina, 2009: 187 fn. 2). Yet it is also possible that the court dismissed the claims on the basis that the claimant's personal rights were not violated.

⁴¹ *Постановление ФАК Московского округа от 12.09.01 по делу N. КГ-А40/4892-01* CDN50, *Постановление ФАК Московского округа от 16.05.02 по делу N. КГ-А40/3007-02* CDN66.

Nevertheless, it is worth highlighting a number of general points here that cast doubt over the observation that the courts have used the rights and interests requirement to deny shareholder standing ‘via the back door’. First, at least in cases where the additional grounds feature in the judgments it suggests that the FAC has considered the cases on their merits. This is inconsistent with the de facto bar interpretation of the rights and interests requirement.

Second, the evidence and arguments used by the proponents of the view that the courts have used the requirement in such a controversial manner does not stand up to a closer scrutiny. Thus, Gudieva appears to be the sole commentator to have raised this criticism. Had the requirement indeed become an ‘insurmountable obstacle’ to shareholder claims other commentators might be expected to have raised similar concerns. It is also notable that Gudieva’s conclusion is based on the fact that the formulation – ‘the claimant failed to prove which of his rights were infringed’ – is invariably repeated verbatim by the arbitrazh courts in their judgments. However, even accepting the inference at its face value, Gudieva concedes that the practice is not uniform (2007: 47). More importantly the inference amounts to no more than the presumption that the judicial statements in fact amount to the de facto bar interpretation.

Actual examination of the cases would be necessary to substantiate the inference and in this respect her analysis is lacking. In particular, the FAC case that Gudieva cites in support of her position as representative of the judicial practice falls short of confirming that the courts adhere to the de facto bar interpretation. The case in point is *Постановление ФАК Московского округа от 25.02.03 по делу N. КГ-А41/8816-02* CDN80 (Gudieva, 2007: 47). In this case the claimant shareholder sought to rescind a transfer of two trucks between the two defendant firms on the ground that the firms had a common director and no requisite section 83 approvals were obtained. The first and the appellate instances courts invalidated the sale and ordered restitution. The FAC struck down both judgments, sending the case for a retrial to the first instance court. In doing so, the court observed as follows:

‘In accordance with the provision in article 4 APC RF only the persons whose rights and legal interests are usurped or disputed can petition for the judicial protection... The claimant did not state which of its rights were infringed and which adverse consequences followed from the transaction’.

A number of observations can be made regarding the decision. First, the court’s reference to ‘adverse consequences’ is consistent with the economic harm interpretation of the rights and

interests requirement – proof of losses is necessary to obtain the restitution. Albeit, as was suggested above, this is not a conclusive indication that the court did not rely on the de facto bar interpretation, the judgment nonetheless does not offer an unambiguous example of the court's apparent insistence that the claimant's personal rights be violated for the action to succeed. Second, the court ordered a retrial rather than dismissed the case outright and therefore provided the claimant with an opportunity to make submissions as to its rights and interests. To this extent any inferences as to what the court would have required the claimant to show to discharge the requirement can only be speculative since no such submissions were made before the courts. Last, but not least, the court found two errors in the lower courts' decisions that could only be rectified at the retrial. The case materials contained no evidence that the claimant held shareholding in the transferor at the time of the transaction. In addition, the lower courts invalidated the secured loan agreement between the two firms – in discharge of which the title to the trucks was transferred to the transferee – without specifying the legal basis for doing so and despite the fact that the claimant only challenged the validity of the transfer and not of the loan itself in its pleadings. It is fair to suggest then that the decision's support for the proposition that the courts have used the rights and interests requirement to de facto bar shareholders' action is at best speculative.

A better example of the court's restrictive interpretation of the requirement is offered by Dobrovolskii, although he does not share the view that it amounts to the denial of the *locus standi* (2006: 179). He cites *Постановление ФАС Московского округа от 16.03.04 по делу N. КГ-А40/1429-04-1,2* CDN115 noting that the judgment provides 'a universal formulation [of the doctrine] applicable to all cases in this category' (2006: 185, 186).

In this case, the FAC held that the lower courts erred in accepting the claimant's argument that the challenged transaction, a sale of property, infringed its right to receive dividends from the company's profits, which, it was argued, were affected by the transaction. The court observed as follows:

'A company, even when profitable, may take a decision not to pay out dividends. Dividends are not a guaranteed source of income for shareholders... A shareholder's interest in holding a transaction ... invalid for infringing his rights and legal interests must be proved as well as asserted. The claimant did not provide the court with any evidence that prior to the transaction he received dividends, and that after the transaction the payments were reduced or ceased.'

It is also clear from the judgment that the court was not referring to the requirement's economic harm interpretation. The court appointed independent valuation concluded that the property's value was RUB 4.9 million whereas it was sold for RUB 1.4 million. The transaction was clearly carried out at a loss.

However, despite the harsh *dicta*, the judgment does not support the de facto bar interpretation. The claimant alleged that the general meeting approval was necessary because the transaction exceeded the two percent of the firm's balance sheet value threshold stipulated in section 83(4) JSCA. The FAC sent the case for a retrial to the first instance court on the ground that the wrong balance sheet had been used to ascertain whether the two percent threshold had been breached. The rights and interests reasoning was arguably immaterial to this outcome and this is also supported by four further judgments that involved the same parties as in the instant dispute, however, challenging different property sales.

In two judgments, *Постановление ФАК Московского округа от 24.02.04 по делу N. КГ-А40/599-04* CDN111 and *Постановление ФАК Московского округа от 25.02.04 по делу N. КГ-А40/811-04* CDN112, the FAC similarly sent the cases for retrials on the ground that the wrong balance sheets had been used to determine whether the two percent threshold had been crossed. In both judgments the court made no reference to the breach of rights and interests requirement. If the requirement was immaterial in these cases, undoubtedly it was similarly immaterial in the case cited by Dobrovolskii, which involved essentially identical facts.

In the remaining two cases, *Постановление ФАК Московского округа от 29.03.04 по делу N. КГ-А40/2053-04* CDN116 and *Постановление ФАК Московского округа от 01.06.04 по делу N. КГ-А40/4080-04* CDN124 the correct balance sheets were used. In both cases the FAC upheld the lower instance courts judgments to invalidate the challenged property sales stating, in the former case, that the claimant's written statement provided sufficient explanation of how his rights and legal interests had been infringed, and more explicitly, in the latter case, that 'the disputed transaction infringes the rights and legal interests of the claimant because ... as the result of the transaction [the first defendant] lost a material base to conduct its economic activity and receive profits, which lead to the devaluation of the claimant's shares and the loss of the opportunity to receive dividends'. The two cases suggest very persuasively that had the correct accounts been used in the case Dobrovolskii

cites the FAC would have invalidated the transaction, rather than sending the case for a retrial.

Finally, the FAC has struck down the lower instance courts' judgments that have attempted to interpret the rights and interests requirement in a manner tantamount to a denial of the shareholder *locus standi* in section 84 invalidity claims. Thus, the court has held that section 84 is an imperative norm that unambiguously grants shareholders the right to challenge the validity of the related party transactions and that, therefore, article 4 APC had to be construed in compliance with the section 84 enforcement right.⁴²

It is noteworthy that the FAC thought the express shareholder standing under the section circumscribed the courts' ability to interpret the breach of rights and interests requirement restrictively. It suggests that the position may have been different prior to the August 2001 reform and there are decisions featuring the requirement prior to the reform taking effect in 2002.⁴³ The *dicta* indicates that the amendment of section 84 may have curtailed the court's ability to deny shareholders the right to bring actions under the section both explicitly and by means of the rights and interests requirement, which may also explain the rise in the shareholder litigation before the FAC in 2003. To recall the statistics given in the Chapter's introductory section, in 2003 the shareholder claims adjudicated by the FAC increased by 175 percent in contrast to the 25 percent increase in the total number of cases decided by the court decided that year. The discussion, therefore, now turns to examine this sudden increase in shareholder actions.

It is submitted that there is an explanation that can account for the increase other than the section 84 amendment. And it is possible to go further and suggest that the alternative explanation is the most likely explanation for the increase in the shareholder actions heard by the FAC over and above the general rise in disputes before the court. Two factors underpin the explanation. The first factor is the absence of the 'proper plaintiff' and the 'wrongdoer control' principles in the Russian related party transactions jurisprudence. In Russia, as will become evident from the case data, shareholders can bring suits under Part XI JSCA when

⁴² *Постановление ФАС Московского округа от 31.10.03 по делу N. КГ-А40/8334-03-1,2* CDN100; *Постановление ФАС Московского округа от 17.11.05 по делу N. КГ-А40/11191-05* CDN148.

⁴³ Two shareholder cases were dismissed under the rights and interests requirement before section 84 was amended. *Постановление ФАС Московского округа от 09.11.00 по делу N. КГ-А40/5072-00* CDN44 and *Постановление ФАС Московского округа от 19.09.01 по делу N. КГ-А40/5121-01* CDN57.

the company is not under the wrongdoers' control, in other words, when the company's management organs are not conflicted in deciding whether to sue and indeed when they have determined that an action is appropriate. This, however, is only part of the explanation. The fact that individual shareholders can sue absent the wrongdoers' control of the company does not account for why shareholders would choose to sue in such circumstances. Why would shareholders seek to intervene, especially given the collective action problem set out above, when the management has already committed to pursuing the litigation?

Thus, the second factor is the companies' inability to proceed with the litigation. Albeit the controllers are willing to sue they cannot bring an action in the name of the company because the law prevents the company from doing so. The law in question is the statute of limitations as applied by the FAC in the company Part XI JSCA litigation. As was discussed in the preceding Chapter, the contract-based standard used by the FAC to attribute the company claimants with the knowledge for the purpose article 181(2) of the RF Civil Code prevents companies from challenging related party transactions outside the one-year period from their completion. However, the controllers' inability to mount the corporate action does not, without more, preclude them from pursuing the same claim in the name of a shareholder. All that is necessary is to find a 'sympathetic' shareholder who would 'lend' her name to the action.

In the United States, for example, it has long been accepted that the derivative actions are often pursued by nominal shareholder claimants who have insignificant stakes in the company and little interest in the outcome of the litigation and who are selected for this purpose *ex post facto* by private attorneys that have a genuine interest created by their success fees to seek out and pursue the wrongdoing through the courts (Parkinson, 1993: 241, 242; Coffee, 1986). If the US lawyers are able to recruit such shareholders so can the controlling shareholders and their appointee management in Russia who are arguably in a better position to do so. Indeed, the controlling 'inside' shareholders can simply bring claims in their own names rather than in the name of the company.

The case data confirms this state of affairs. In 11 out of 22 shareholder cases heard by the FAC in 2003 'defendant' firms that were a party to the disputed transactions supported the shareholders' claims. Doubtless, but for the statute of limitation these firms would have filed the claims themselves and the FAC would have heard only the remaining 11 shareholder

claims in 2003: an increase of 38 percent on 2002, rather than 175 percent, which is arguably closer to the 25 percent general increase in judgments the FAC issued that year.⁴⁴

There is more difficulty with explaining the 22 shareholder cases examined by the FAC in 2004 because the firms supported the shareholders' actions only in five cases. In other words, in 2004 there were 17 'genuine' shareholder claims opposed by the companies, which represents a 55 percent increase on the number of such claims in 2003 and contrasts with the smaller, 16 percent,⁴⁵ increase in the litigation before the FAC in 2004. However, the figure is skewed by seven judgments that arose from two disputes (five judgments relate to one⁴⁶ and two to the other⁴⁷) and that involved the same parties albeit challenging separate transactions. And if the seven judgments are treated as two for the purpose of ascertaining the number of the 'genuine' shareholder claims then the figure becomes 12, which is one judgment more than the figure for the year 2003.

Conclusion

To sum up the discussion on the individual shareholder standing, it appears that the FAC has allowed individual shareholders standing to rescind the transactions completed in contravention of Part XI JSCA both before and after the August 2001 reforms. Furthermore, the court has permitted the standing despite the JSCA drafters' reservations on the issue. *Prima facie* the FAC jurisprudence casts doubt over the suggestions that the judiciary has undermined the position of the investors and thereby halted the development of the Russian equity market. Had the court been minded to bar shareholder actions it could have easily interpreted the legislation prior to the August 2001 reforms taking effect to achieve this outcome and yet it has not done so.

⁴⁴ There were no 'wrongdoer not in control' shareholder cases in 2002, therefore not affecting the comparator percentages.

⁴⁵ The figures are based on the statistics disclosed by the FAC on its website <http://fasmo.arbitr.ru:80/fasmo/reports/activity/293.html>. Accessed on 14 July 2010. Due to the webpage no longer being available online a hardcopy of the webpage has been included in Appendix 1 p.p. 13a, 14a.

⁴⁶ *Постановление ФАС Московского округа от 24.02.04 по делу N. КГ-А40/599-04* CDN111; *Постановление ФАС Московского округа от 25.02.04 по делу N. КГ-А40/811-04* CDN112; *Постановление ФАС Московского округа от 16.03.04 по делу N. КГ-А40/1429-04-1,2* CDN115; *Постановление ФАС Московского округа от 29.03.04 по делу N. КГ-А40/2053-04* CDN116; *Постановление ФАС Московского округа от 01.06.04 по делу N. КГ-А40/4080-04* CDN124.

⁴⁷ *Постановление ФАС Московского округа от 07.04.04 по делу N. КГ-А40/1043-04* CDN117; *Постановление ФАС Московского округа от 30.04.04 по делу N. КГ-А40/3196-04* CDN123.

To be sure there is some uncertainty over the court's references to the rights and interests requirement in the case data. However, the evidence offered in support of the proposition that the courts have used the requirement as an alternative means to proscribe shareholders' standing is hollow. Generally, it does not appear from the FAC case data that the court has barred shareholders' claims either explicitly or 'via the back door'. Of course, it is possible that the RTS rally experienced during the period following the August 2001 reforms could be partly attributed to the section 84 amendment. But it is much harder to attribute the rise to any possible under-enforcement by shareholders occasioned by Russian courts in the light of the case data. As shown above, the case data suggests that the post 2002 disproportionate increase in shareholder litigation under Part XI JSCA appears to be attributable to the strict statute of limitations in company claims rather than the section 84 amendment.

Finally, it is worth posing a separate but nonetheless pertinent question regarding the actions brought by shareholders that are supported by the defendant firms. The question is, why did the FAC sanction such litigation for it defeats the objectives of the strict statute of limitations in the company claims that were set out in the preceding Chapter? The reduction of opportunistic litigation, the incentives to improve the internal controls and the channelling of litigation by distressed firms under the insolvency legislation arguably become eliminated if the companies are permitted to circumvent the statute via the shareholder actions.

In the author's opinion, there are three principal answers to this question. First, barring such claims increases the risk of strategic behaviour by the companies and their controllers. The sole fact that the controllers decide to open proceedings does not dissolve the concerns about their conflicts of interest. For example, it is accepted that companies and their controllers may decide to commence litigation but assign inadequate resources for that purpose.⁴⁸ As Kershaw explains, 'regulators need to be wary of board controlled litigation where the board's direct and indirect conflicts undermine the successful pursuit of litigation. In such cases the company could end up with the worst of all possible worlds: a low likelihood of success but the incurrence of significant legal and opportunity costs' (2009: 537). In this light, the consequences of the courts in Russia striking out the shareholder actions that are supported by the companies and that are brought outside the contract-based statute of limitations are readily foreseeable. The controllers of a company faced with a shareholder

⁴⁸ See comments on the UK Companies Act 2006 section 262 (Kershaw, 2009: 537, 538, 567, 568).

action could strategically plead in support of the action to have it dismissed under the statute of limitations.

Second, such jurisprudence is unlikely to prove effective in the enforcement of the statute of limitations applicable in the company litigation. Arguably it will be a matter of time before the companies and their legal advisors figure out the perils of supporting shareholder actions and shift to strategically pleading notional defences in opposition to the actions, or making no submissions at all, while in the actuality instigating and sponsoring the claims. Third, the FAC has sought to curtail the ability of companies to overcome the statute through shareholder actions, albeit imperfectly. As discussed below, the court has used the statute applicable in the company litigation in the claims brought by the controlling inside shareholders.

The statute as well as the contemporaneous ownership rule developed by the FAC in the shareholder section 84 actions are considered next.

CHAPTER 5

PROCEDURAL RULES IN SHAREHOLDER ACTIONS

Introduction

Procedural rules impose constraints on shareholder actions and therefore by definition depart from the investor protection principle. The law would accord the minority shareholders a greater degree of protection if the procedural rules were absent. As such procedural rules developed by the FAC require a justification on the basis of the aggregate welfare maximisation at least in so far as the legislation and the SAC precedent leave scope for the FAC to develop the rules independently. This is the normative criteria for constructing and testing the judicial bias hypothesis that was introduced in Chapter 2. The two procedural rules that feature in the case data are the statute of limitation and the contemporaneous ownership rule and it is with the analysis of these two rules that this Chapter is concerned.

Earlier, section 4.1 outlined the arguments in support of restraining minority shareholder actions by means of procedural rules. It suggested that, on the one hand, the sharing of the recovery puts small shareholders off from incurring costs in pursuit of actions with net expected gains to the shareholders as a whole. On the other hand, the sharing of the costs of litigation incentivises small shareholders to bring claims in pursuit of some collateral benefit irrespective of whether the claim carries net expected gains or losses to the shareholders as a whole. As explained above, the principal concern with litigation brought by minority shareholders is the risk of it being contrary to the interests of the shareholders as a whole.

The more common procedural rules respond to this problem by allocating litigation rights to shareholders with a sufficiently large stake to more fully internalise the cost-benefit calculus of bringing a claim or to another agent capable of the same and whose judgement is not tainted by conflicts of interest, such as a court (Davies, 2008: 611; Reisberg, 2007: 83). As will become apparent from the discussion below, neither the statute of limitations nor the contemporaneous ownership rule achieve this objective. Nevertheless, the statute of

limitations and the contemporaneous ownership rule can create net gains for the parties' welfare. In particular, it will be argued below, that certain constructions of the two rules incentivise the controlling shareholders to disclose related party transactions to the shareholders. In doing so, the rules attend to the adverse selection problem, which, as explained in Chapter 2, currently provides the most influential theoretical account for the underdevelopment of the stock markets and to this extent the rules may, at least in theory, contribute to the development of the Russian equity market.

Thus, the ensuing analysis identifies different permutations of the rules and assesses their conformity with the welfare maximisation. The analysis shows that the rules can lead to net joint welfare gains provided the courts tailor the rules to reflect the characteristics of different types of claimants. In this regard, the key characteristic is the claimants' access to the internal corporate books and records. On this basis it will be argued that the efficient construction of either rule differs for the minority outside shareholders who do not have such access and for the inside shareholders who do. The analysis concludes by examining to what extent the FAC jurisprudence adheres to the predictions of the welfare maximisation analysis.

5.1 Statute of limitations

5.1.1 Introduction

The analysis of the legislation as well as the SAC and the RF Constitutional Court precedent on the statute of limitations applicable in the section 84 suits was already carried out in Chapter 3. The academic commentary on the statute was also examined in that Chapter. Hence, an outline of the key themes of that analysis is sufficient for the purposes of the present section.

It will be recalled that the statute is to be found in article 181 of the Civil Code and that it differs for void and voidable transactions. All the shareholder claims that failed under the statute of limitations were decided after the FAC began to characterise related party transactions as voidable. For this reason, the ensuing analysis is concerned only with the statute applicable to the voidable transactions. The statute of limitations for such transactions is in article 181(2) of the Code. It provides for a one-year prescription period, which is triggered on the date when a claimant discovered, or should have discovered, the

circumstances indicating the invalidity of the challenged transaction. The Code's article 199(2) further provides that a court can dismiss claims for the expiry of the statute of limitations only on the application by a party to the dispute.

The drafting of article 181(2), '*when a claimant discovered, or should have discovered*' the relevant circumstances giving rise to a cause of action, provides for the actual and a constructive standard of attributing the knowledge to claimants. To this extent the Code explicitly envisages judicial departures from the actual knowledge standard albeit without specifying a permissible scope of such departures. As was suggested in Chapter 3, the actual knowledge standard, although arguably the more accommodating standard for the claimants, poses considerable difficulties of verifiability for the courts in that since only the claimants are the true purveyors of their knowledge they would always maintain the lack of the relevant knowledge at such time that could lead to the dismissal of their claim under the statute. Invariably, therefore, the courts have to infer the claimants' knowledge from the objectively ascertainable and verifiable circumstances meaning that in practice the majority of the article 199(2) petitions turn on the consideration of what verifiable circumstances are presented in the parties' evidence and whether such circumstances are sufficient to construe the claimants as having been put on notice of their causes of action at a stage over a year prior to the bringing of their actions, in other words, on the interpretation of the constructive knowledge limb of article 181(2).

The Code does not add any substance to the constructive knowledge standard beyond the reference to the term '*should have discovered*'. Such further substance was provided by the Constitutional Court in April 2003 which held that the start of the limitation period must commence from the moment when the claimant '*had a real opportunity to discover*' that the cause of action existed.¹ However, as was explained in Chapter 3, with arguably limited success in that neither the Court nor the SAC (nor the commentators) explained what the '*real opportunity to discover*' entailed. The commentators have used the Judgment to criticise the jurisprudence that inferred the requisite knowledge from the date of a transaction's completion – the contract-based knowledge standard – but without explaining from which point in time the courts ought to infer the existence of the knowledge. The analysis in Chapter 3 challenged this criticism on the basis that, on the one hand, to the extent the Judgment might be taken as censuring the contract-based standard it only did so in respect of

¹ *Постановление Конституционного Суда Российской Федерации от 10.04.2003* para. 5.2.

the claims brought by the minority outside shareholders and, on the other, that the contract-based standard could lead to the gains in the parties' welfare when applied to other types of claimants namely, the companies that were party to the impugned transactions.

Section 5.1.2 considers first, whether the contract-based standard is also justifiable on the efficiency grounds in shareholder claims. It argues that it is, provided the courts confine the standard to the claims brought by the controlling inside shareholders. Second, it considers which knowledge standard could maximise the joint welfare of the parties in relation to the minority outside shareholder-claimants. It attempts to fill the void in the literature by suggesting two alternative standards that the courts could apply in relation to such claimants and examines which of the two standards is more likely to be the welfare maximising legal norm. Third, the section considers the implications for the analysis from the relative ease with which the controlling shareholders can avoid the contract-based standard by bringing claims ostensibly as minority shareholders. Subsequent sections (5.1.3 and 5.1.4) summarise the analysis to formulate a falsifiable hypothesis and test the FAC judgments against it.

5.1.2 Analysis

Insider claims: the contract-based standard

The analysis in Chapter 3 criticized the literature's outright rejection of the contract-based standard in relation to *every* claimant for not having a foundation in the law. On the contrary, that analysis sought to demonstrate that in the company actions not only was the standard reconcilable with the 'real opportunity to discover' doctrine of the Constitutional Court but also that it was the more likely norm to maximize the joint welfare of the parties. In this section it will be argued further that the same is likely to be the case in relation to certain shareholder actions namely, the actions brought by the inside shareholders.

Undoubtedly, the indiscriminate application of the contract-based standard to all the shareholders will not yield the welfare maximising outcomes. Unless related party transactions are disclosed to shareholders, even the minority shareholders with a level of stock ownership sufficiently high to overcome the collective action problem incentive to remain rationally apathetic – the investors whose share of the benefit from rescinding

transactions will outweigh their monitoring and litigation costs – may not have the requisite access to corporate information to detect the transactions within a year from them taking place. What is more, the standard would make the monitoring task all the more difficult because it would create the incentives for the controlling shareholders to camouflage expropriation. Since transactions undetected within a year from them taking place will effectively become judicially unreviewable, the rational response for the controlling shareholders would be to reduce the probability of their detection during that year. Arguably, the indiscriminate application of the contract-based standard would be tantamount to a non-intervention regime, failing both to deter the minority expropriation and to incentivize the revelation of information to the investors with the self-evident effect on the Russian equity market.²

Yet, in a sub-set of section 84 shareholder actions the contract-based standard could result in the net gains to the parties' welfare. This sub-set of cases is the actions brought by the inside shareholders. Ordinarily, on the one hand, where such shareholders hold controlling stakes they are unlikely to challenge transactions that expropriate the minority for the benefit of themselves. It is fair to suggest that the welfare losses, either from the underdeterrence of minority expropriation or from the reduction in the information concerning conflicts and transactions revealed to the minority that might follow from restricting section 84 actions by the controllers, are likely to be fanciful.

On the other hand, in respect of the actions to redress overreaching that may have joint welfare effects beyond the fanciful, namely actions attacking the transactions involving the 'rogue' directors that expropriate both the controllers and the minority alike, the controllers will have the access to the necessary corporate information to detect the wrongdoing by virtue of their power to appoint the majority of the board, the management, the internal inspectors and external auditors. In these cases, the failure to file the section 84 suit within a year from the suspect transaction taking place will arguably have more to do with the lapses in the internal control machinery than with the controllers' inability to obtain corporate books and records or the collective action problem. Indeed, holding the controlling shareholders to

² The only constraint on expropriation in this case would be the financial market forces if it is envisaged that the company will return to the market to raise additional funds. However, even this argument relies on the fact that the transaction will be ultimately discovered. To rephrase Easterbrook and Fischel's observation 'investors won't be fooled twice, only if they are aware that they were fooled on the first occasion'.

the contract-based standard under article 181(2) would create the ‘efficient precaution’³ incentives for the controllers – the incentive to expend resources on the improvement of the internal control function until the marginal cost of the precautionary measures equals the reduction in the expected losses from the ‘rogue’ director expropriation, the marginal benefit.

It should be apparent that this argumentation echoes the economic analysis of the contract-based standard in the company actions set out in Chapter 3 of this thesis. In that Chapter it was argued that where solvent company actions are brought without a prior change of control the standard is efficient because, on the one hand, it reduces the likelihood that opportunistic claims will be filed and removes the need for the courts to rely on unverifiable information; and, on the other hand, it creates the incentives for the efficient precaution of the expropriatory related party transactions involving rogue directors. Because, as explained above, the ‘proper plaintiff’ and the ‘wrongdoer control’ principles are absent in the Russian section 84 jurisprudence such shareholders will have a choice whether to bring the section 84 invalidity claims in their own name or in the name of the company. But for the statute of limitations, there are no material differences between the two claimants.⁴

On this basis, the statute of limitations should apply to controlling shareholders on the same terms as it applies in the company suits with the contract date set as the trigger for the one-year limitation period. Otherwise, permitting the controlling shareholders to mount the section 84 suits in circumstances when the company cannot, i.e. outside the one-year period from the date when the transaction was executed, would annihilate the welfare gains created by the statute of limitations in the company suits. If the controlling shareholders can ‘bypass’ the statute of limitations by bringing the claims in their own name the opportunistic litigation will not recede and the incentives for efficient precaution of the expropriation by rogue directors will diminish. In these cases the contract-based standard in effect provides a functional equivalent to the ‘proper plaintiff’ and ‘wrongdoer control’ principles absent in Russian jurisprudence. It prevents a controlling shareholder from suing in the circumstances where the company is also unable to sue because of the statute. Put short, if the contract-

³ The term ‘precaution’ is used broadly in economic theory as any action that reduces harm (Cooter, 1985: 3).

⁴ The controlling shareholders would prefer to bring a corporate claim because the litigation costs will be shared among all the shareholders. However, if the corporate claim is barred on the ground of statute of limitation, the controlling shareholders will bring the claim in their own name as long as litigation costs outweigh their pro rata benefit from the rescission of the transaction.

based standard is the welfare maximising norm in the company claims, which as was argued in Chapter 3 it is, then the standard is also the welfare maximising norm in the claims brought by the controlling shareholders. The FAC jurisprudence that applies the contract-based standard to dismiss actions brought by controlling shareholders under the statute of limitations would not support the judicial bias hypothesis.

The difficulty with the above analysis is identifying the shareholding threshold that would qualify a claimant as an inside shareholder so as to attract the application of the contract-based standard. The insiders are likely to exercise *de facto* control over a company with a less than 50 percent shareholding. Such a threshold is arguably too high.⁵ At the same time, an *ex ante* determination of the level of shareholding with the perfect precision to capture only the insiders as a category is impossible due to the likely variation in the firms' ownership structure. The category insider is *prima facie* endogenous, i.e. firm specific, thus precluding the one rule fits all approach.

Nevertheless, as the case data will show, the FAC has set the threshold at 25 percent of a company's share capital. And, it is submitted, correctly because the 25 percent shareholding level is likely to maximize the joint welfare. The reasons are as follows.

First, the threshold is sufficiently low to capture most of the controlling shareholders. Empirical research shows that the average share of the largest shareholder in Russian firms varies, depending on the samples, from 28 to 42 percent (Yakovlev, 2004: 391). Second, and more importantly, the court did not set the threshold arbitrarily. Rather, the threshold is based on the JSCA information access provisions namely section 89(1), which, as was explained above, entitles the 25 percent shareholders to access the internal corporate books and records.⁶ Furthermore, the formal right is buttressed by other JSCA provisions, which provide the 25 percent shareholders with the bargaining power to negotiate access to the internal corporate records. Thus, under the JSCA, the 25 percent shareholders can veto a

⁵ Indeed section 81 JSCA provides for 20% ownership to qualify the shareholder as a related party. In other words it recognises that at this level the shareholder can exercise sufficient control over the company to cause it to execute transactions beneficial to the shareholder.

⁶ This amendment was introduced in August 2001 and came into force in 2002. There was no express right to this additional information prior to the amendment. The arguments in this part will therefore be strongest in relation to cases from 2002 onwards. However, as explained below, the informal channels may have given the 25% shareholders access to this information prior to 2002.

considerable number of corporate decisions that require the special majority voting.⁷ In addition, the 25 percent shareholders will also benefit from the JSCA rights accorded to the substantial shareholders whose holding does not exceed the 25 percent threshold such as the rights to call extraordinary general meetings; to request an internal inspection;⁸ and, in firms with 1000 or more shareholders, to appoint board members under the section 66(4) mandatory cumulative voting provisions,⁹ the latter further augmenting the 25 percent shareholders blocking power in relation to the corporate decisions that require the unanimous board approval.¹⁰ In other words, contrary to what was observed above, in Russia the category of inside shareholder is to an extent determined exogenously by the JSCA thus allowing the court to apply the one rule fits all approach across the board of the Russian joint stock companies.

To be sure, the definition of the ‘inside shareholder’ based on the 25 percent shareholding is not synonymous with the ‘controlling shareholder’. It is foreseeable that there will be firms with shareholders whose stock exceeds 25 percent of the voting share capital but with the

⁷ Section 49(4) requires the following resolution to be passed by 75% majorities: charter amendments; reorganisation of the company; liquidation of the company; determination of the number, nominal price, categories and the rights attached to, declared shares; buy backs of shares. Of these, the voting rights with respect to the increases in declared shares are likely to be the most frequently used as companies cannot issue shares exceeding the number of the declared shares. Every time the company wishes to raise funds in excess of the shares it will have to amend the charter which 25% shareholders will be able to veto. Additionally, section 39(3) requires 75% majority approval for share issues under the closed offers; section 39(4) requires 75% majority for all offers in excess of 25% of the issued share capital; section 79(3) requires 75% majority for substantial property transactions that exceed 50% of the companies balance sheet; section 83(4) requires majority of all non-interested shareholders approval for related party transactions that exceed 2% of the balance sheet – in practice this means that in firms where the controlling interests exceeds 50% +1 shares, the 25% shareholder will have a veto.

⁸ Pursuant to section 85(3) JSCA shareholders holding 10% of a company’s voting shares can require its inspection commission to review and report on the company’s activities. The JSCA provides such commissions with considerable power: companies’ management is obliged to produce internal books and records to the commission and the commission is empowered to demand the convening of an extraordinary general meeting, arguably a meaningful tool to induce managements’ cooperation (section 85(4) and (5)).

⁹ To constrain potential avoidance practices – having smaller boards – section 66(3) requires that in firms with 1000 or more shareholders there be at least 7 board members, in firms with 10000 or more shareholders there be at least 9 board members. Section 53(1) allows 2% shareholders to nominate candidates for board, collegiate and individual management organ, internal auditor etc. For smaller companies section 66(4) states that cumulative voting may be provided for in the charter. The 25 percent shareholders will be able to appoint their representatives to the board in rough proportion to their percentage shareholding. Where a board has 7 members, the 25% shareholder is guaranteed to appoint 2 directors.

¹⁰ Section 79(2) requires unanimous board approval for substantial property transactions valued between 25% - 50% of the balance sheet; section 28(2) requires unanimous board approval to increase share capital, where the board has the decision right.

controlling interest residing in the hands of another: the 25 percent threshold is over-inclusive. Furthermore, such shareholders should have the requisite incentives to monitor the controlling shareholders' conduct and may therefore, as was explained in section 4.1.1, provide the most promising bulwark against the minority shareholder expropriation. Restricting their ability to challenge the related party transactions may therefore carry welfare losses for the shareholders. This means that the approach to the economic analysis adopted above in relation to the controlling shareholders, namely that 'if the contract-based standard is the welfare maximising norm in the company claims, then the standard is also the welfare maximising norm in the claims brought by the controlling shareholders' cannot be simply transposed with respect to the actions brought by the 25 percent holders. The welfare losses from restricting such claimants' right to seek the rescission in relation to transactions that are no more than 'a year old' have to be accounted for in the cost-benefit analysis.

Nevertheless, even assuming that such claimants will opt to scrutinize – rather than collude with – the controlling shareholders, circumscribing their right to seek the rescission by the contract-based knowledge standard would not materially affect the outcome of the cost-benefit calculus. The contract-based standard is likely to remain the welfare-maximizing norm even when applied to a corporate constituency broader than the controlling shareholders – to the 25 percent shareholders.

The most obvious adverse impact of applying the contract-based knowledge standard to the 25 percent shareholders is on the deterrence of the minority expropriation. If the claimants that provide the 'most promising bulwark against the minority expropriation' are unable to bring related party transactions before courts then the controlling shareholders, acting rationally, will increase the level of expropriation – the more likely it is that a controller will get away with diverting an asset, the more likely it is that he will divert it.

The deterrence, however, is a function of the enforcement effort (monitoring) as well as the sanction (rescission) (Cooter and Freedman, 1991)¹¹ and it does not automatically follow that restricting the availability of the sanction to the first year from the transaction's completion would result in the overall decline in the deterrence. On the contrary, the efficient precaution analysis discussed above and in Chapter 3 indicates that the 25 percent shareholders would

¹¹ Accuracy in adjudication is the third factor (Kaplow, 1994).

step up their monitoring effort to increase the probability of detection in year one.

Unlike other minority shareholders, the 25 percent shareholders have the access to the necessary corporate records, leaving their monitoring effort as the only obstacle to the timely detection of the related party transactions. The application of the one-year limitation period to such claimants from the contract date would improve their incentives to monitor the suspect transactions by requiring them to internalize their share of the loss from the inability to rescind the transactions after one-year from them taking place. An efficient level of monitoring will be achieved where the marginal cost of additional monitoring equals the marginal improvement of the probability of rescission in year one.¹² The increase in the enforcement effort, i.e. in the monitoring, would arrest the overall adverse impact on the deterrence and therefore expropriation.

Of course, one cannot be certain that the overall level of deterrence would not fall notwithstanding the increase in monitoring. However, it is likely that it would not, at least not materially. The reason for this conjecture is that if the monitoring effort did not detect the suspect transaction within a year from its completion, it would be unlikely to detect it subsequently. If the transaction comes to light in the year two or three or thereafter, it is more likely to do so due to a chance occurrence, whatever that might be, than as the result of the proactive monitoring effort. Furthermore, the greater the lapse of time the greater are the costs involved in obtaining the rescission (for example, in obtaining evidence or in tracing the asset or its monetary equivalent) and hence the lower the probability of the remedy being sought. This indicates, on the one hand, that a diminution in deterrence caused by the 25 percent shareholders' inability to rescind after a year from the transaction's occurrence is unlikely to be considerable and, on the other hand, that the contract-based standard in effect

¹² A simplified example can help to demonstrate the point. A 50 percent shareholder causes the company to sell an asset worth £200 to himself for £100. A 25 percent shareholder will bear £25 loss on the transaction. Assume that the shareholder can rescind the transaction at no cost so that the detection poses the only obstacle to the rescission. There is a 60 percent probability of detecting the transaction in year 1, and 25 percent in year 2 (assume no year 3 or that probability of year 3 detection = 0). The expected loss from the sale to the shareholder at t_0 is then 0.4 (probability that the transaction would not be detected in year 1) $\times 0.75$ (probability that the transaction would not be detected in year 2) $\times 25$ (the loss) = £7.5. If the opportunity to rescind the transaction in year 2 is withdrawn (i.e. the probability of detection in year 2 = 0), the expected loss on the transaction would be 0.4 (probability that the transaction was not detected in year 1) $\times 25$ = £10. A rational shareholder would expend up to £2.5 on monitoring to improve the probability of detection in year 1. The efficient level will be achieved where an additional penny spent on improving monitoring does not yield an increase in the probability of detection in year 1.

converts the passive benefit of the ‘chance discovery’ and the rescission into the incentive to invest resources into the proactive monitoring effort.

Finally, and crucially, should a related party transaction come to light outside the one-year period it does not mean that it will be immune from the judicial review solely because shareholders with the 25 percent holding are unable to bring it before the court. Shareholders with a smaller holding are not precluded from bringing the section 84 actions by the contract-based standard applicable to the 25 percent shareholders. Certainly the incentives to remain passive occasioned by the collective action problem grow stronger as the level of shareholding of the potential litigants declines. But surely the 25 percent threshold is sufficiently high to exclude the vast majority of the substantial and institutional investors – the shareholders who have sufficient investment in a firm to overcome the collective action incentive to remain passive – from its purview.¹³

Outsider claims: disclosure-based standard

If, as argued in the preceding section, the contract-based standard is congruent with both the Constitutional Court’s ‘real opportunity to discover’ test and the welfare maximisation criterion when applied to claimants with a shareholding in excess of 25 percent, it is likely to fail in both the respects if applied to claimants with a lower level of shareholding. Claimants’ ability to detect the undisclosed related party transactions, i.e. their access to the internal company records, is the pivotal justification for applying the standard and this justification is absent when it comes to the smaller minority shareholders. If not the contract-based standard, then what standard for attributing knowledge under article 181(2) would meet both the Constitutional Court’s test and the efficiency criteria in relation to such claimants? As was explained in Chapter 3, the legislature, senior courts and the literature have not, so far, offered an answer. The task is pursued in this section.

The section introduces two alternative standards for attributing knowledge to the minority outside shareholders under the article 181(2) statute of limitations. For convenience, the two

¹³ This is also supported by empirical studies of institutional investors’ shareholding in Russian firms. Thus, one study shows that investment funds had an average of 19.2% of shares in companies where they owned shares (Earle, 1998: 12, 13). A more recent study of the ownership structure in the RTS-listed firms found that the average voting rights of the institutional investors in the sample firms was 10.06% (the median was 9.6%) (Chernykh, 2008: 180).

standards will be referred to as the receipt-based standard and the disclosure-based standard. Having defined the two standards, the section embarks on the economic analysis of the standards in order to ascertain the standard that is more likely to maximise the aggregate welfare of the parties. As will be explained below, the two standards differ in the evidence that the article 199(2) petitioner, invariably the party seeking to uphold the disputed transaction, has to put before the court in order to dismiss the claim under article 181(2). The analysis of the possible constructive knowledge standards through the evidential lens – what the parties are required to demonstrate – transcends the linguistic contortions of the legal terms ‘should have discovered’ and ‘a real opportunity to discover’ by injecting them with objective criteria thus making the economic analysis, and ultimately the formulation of a falsifiable hypothesis, possible.

It was observed in sections 3.3.2 and 5.1.1 above that claimants’ actual knowledge of transactions and conflicts that form the basis of the section 84 suit is unverifiable enabling them to maintain no knowledge of the relevant facts at such time as would lead to the striking out under article 181(2) whenever an article 199(2) petition is made. No rational claimant would make admissions that will lead to the dismissal of the claim, meaning that invariably article 199(2) petitions turn on a constructive knowledge standard. Certainly there may be instances where an article 199(2) petitioner will be able to demonstrate that the claimant was actually aware of the relevant facts over a year prior to the bringing of the claim by showing, for example, that the claimant participated in a general meeting where the transaction’s details were discussed. However, even in such instances the courts in fact would be applying a constructive knowledge standard – drawing an inference that the presence at the meeting entailed knowledge of the transaction and a conflict therein. It is not the knowledge (the unverifiable) but the physical presence (the verifiable) that determines the court’s decision.

Similarly, where an annual report disclosing the particulars of a related party transaction is sent to a shareholder by registered post and the shareholder signs for the envelope at the point of delivery, it is the signature rather than the shareholder’s knowledge that determines the judicial outcome. In such circumstances, it would be open to the shareholder to argue that she left the room when the transaction was discussed or that she did not open the envelope but these arguments are unlikely to be persuasive with the court. The probability of the claimant having the actual knowledge is high and it is difficult to imagine what more the company could have done to put the shareholder on notice that would not be prohibitively costly. In these circumstances it is difficult to reasonably dispute that the claimant had ‘a real

opportunity to discover' and 'should have discovered' that a transaction involving a conflict of interest took place.

The constructive knowledge standard that requires the article 199(2) petitioners to demonstrate the physical receipt of the relevant information by the claimant will be referred to as the receipt-based standard in the ensuing discussion. Arguably, short of the judicially inaccessible actual knowledge standard, the receipt-based standard is the most claimant friendly, and therefore the most congruent with the investor protection principle, interpretation of the article's 181(2) constructive knowledge limb. Under the standard, claimants would only need to submit that they had no knowledge of transactions and conflicts. If the article 199(2) petitioners are unable to adduce evidence of the physical receipt of the relevant information, the claimants would win the statute of limitations point and the disputes will be adjudicated on their merits.

An alternative to the receipt-based standard is the disclosure-based standard. The standard involves commencing the article 181(2) period from the date the transaction and the conflict of interest were disclosed in corporate documents available to shareholders. Under the standard, rather than having to demonstrate that the claimant received the relevant disclosure, the article 199(2) petitioner need to show that corporate documents disclosed the transaction and the conflict. The court will dismiss the claim where it is satisfied that both items were adequately revealed by the disclosure, unless it is shown that the documents were not accessible to the claimant.

Similarly to the receipt-based standard, the disclosure-based standard does not require the courts to consider unverifiable information. The courts will only need to ascertain what disclosure was made and when. However, to the extent the standard establishes an additional burden on shareholders challenging the validity of related party transactions – claimants will have to demonstrate that they had no access to the documents containing the disclosures to prevent the dismissal of claims – it departs from the investor protection principle. As such the judicial recourse to the disclosure-based standard would *prima facie* support the judicial bias hypothesis, unless the standard could be justified on the efficiency grounds. In other words, if, given the choice of the two standards, the disclosure-based standard is the welfare maximising norm. The remainder of the section argues that it is.

The primary reason for thinking that the disclosure-based standard is the welfare maximising standard for attributing knowledge to the minority outside shareholders under the article

181(2) limitations statute is that it creates incentives for the efficient disclosure of transactions and conflicts of interest therein. The following analysis explains, first, how the disclosure-based standard incentivises the disclosure; second, how the receipt-based standard fails to provide the same incentive; third, how the potential welfare losses from the disclosure-based standard – that is the forgone benefits of the receipt-based standard – are unlikely to outweigh the efficiency gains from the incentive to reveal information created by the disclosure-based standard.

Thus, in Chapter 2 it was explained that gap-filler rules that encourage revelation of information, referred to as the ‘information-forcing’ rules or the ‘penalty defaults’, can be optimal (Ayres and Gertner, 1989; Bebchuck and Shavell, 1991, 1999; Schwartz, 1992: 282). Such rules operate by placing the better-informed parties at a disadvantage if they do not disclose a particular item of information and are considered efficient because they improve pricing (Ayres and Gertner, 1989; Cheffins, 1997: 298; Deakin and Hughes, 1999: 18). Specifically in the corporate law context, Coffee famously argued that ‘the optimal default rule is ... the rule that best compels each party to reveal to the other its intended use of discretionary powers ... [because] it forces those possessing private information to disclose it to the market – and hence results in more accurate pricing’ (1989: 1623),¹⁴ provided however that any opt-outs from the strict fiduciary duty are transaction specific. As he explained, only when an opt-out provision is limited to a specific transaction, ‘the market can judge more accurately the likely diversion of funds that has been authorized’ (1989: 1668).

It is readily apparent that the disclosure-based standard is an example of an information-forcing rule. A related party transaction will become immune from the invalidity after one year from the date all the relevant facts were disclosed to the shareholders. Related party transactions that are not so disclosed will carry the risk of invalidity indefinitely. Corporate insiders that fail to make the requisite disclosure are therefore placed at a disadvantage to those that do. Since the necessary disclosure is of the circumstances of the cause of action – the transaction and the conflict of interest – the standard also meets Coffee’s transaction specificity requirement. Furthermore, the information revelation advantage of the standard is augmented by the deficiency of the Part XI JSCA and other disclosure rules in Russia to provide optimal incentives to disclose related party transactions. Indeed, on this basis the analysis in Chapter 2 concluded that a gap-filler rule that could induce the disclosure at a

¹⁴ See also Cheffins, 1997: 298 – 301, Deakin and Hughes, 1999: 19, 20; Easterbrook and Fischel, 1993: 445; Whincop, 2001: 76-78.

lower cost than Part XI JSCA (Bebchuck and Shavell, 1991: 286, 291, 292, 301 – 303), the rule that could therefore incentivise more disclosure, would be *prima facie* efficient.

Of course the receipt-based standard for attributing knowledge under the statute of limitation can also be conceptualised as an information-forcing rule. The receipt of the relevant disclosure by shareholders will forestall challenges to the disclosed transaction after a year from the date the disclosure was received, thus, at least in principle, also providing the controllers with the incentive to directly communicate the fact of the transaction and the conflict to the shareholders.

However, the receipt-based standard falls prey to one of the central obstacles to the information-forcing rules yielding optimal outcomes. The obstacle is the transaction costs: information would only be revealed if it is not too costly to do so.¹⁵

It is foreseeable that the transaction costs of the disclosure are likely to be prohibitive under the receipt-based standard. To protect transactions from subsequent challenges, companies and their controllers would have to obtain sign offs from every shareholder acknowledging the receipt of the relevant corporate disclosure documents. The standard would effectively operate as an approval process save that the sign off would be required from every shareholder. In firms with a large shareholder body this will be physically impossible. Moreover, the daily turnover of shares on stock exchanges entails that the sign off will lose its value every time shares change hands: new shareholders will be able to maintain that they did not receive the disclosure. Arguably, it would be less costly to protect the transaction by calling a general meeting and seeking the approval of a majority of non-conflicted shareholders pursuant to Part XI JSCA. In other words, the receipt-based standard would not induce the disclosure at a lower cost than Part XI JSCA and would not improve on the volume of disclosure than would otherwise follow in the absence of the standard.

In contrast, the transaction costs under the disclosure-based standard are likely to be considerably smaller. The disclosure can simply be incorporated in the documents routinely published by the firms such as the annual and quarterly reports. The disclosure-based standard is likely to incentivise more disclosure than the Part XI approval process and hence also the receipt-based standard.

¹⁵ Armour and Whincop, 2007: 435; Ayres and Gertner, 1991: 761; Cheffins, 1997: 299, 300; Easterbrook and Fischel, 1993: 445.

Would the benefit of the potentially greater level of disclosure of transactions and conflicts occasioned by the disclosure-based standard outweigh the costs of departing from the investor protection principle? Intuition suggests that it would. Given that in Russia the investor protection is the guiding principle behind corporate legislation because of its, supposed, positive effects on the stock market development, which is afflicted by the adverse selection problem – the investor’s inability to distinguish between issuers that will and will not engage in expropriation – it is likely that the disclosure-based standard in incentivising the disclosure of related party transactions over and above that would otherwise follow under Part XI JSCA and the receipt-based standard could improve the investors’ ability to distinguish between the issuers along the ‘expropriator – not expropriator’ dichotomy. In doing so the disclosure-based standard would have positive implications for both the efficiency and the investor protection. Adverse selection is a problem of pricing and it is the pricing that greater disclosure is meant to improve.

Nevertheless, for completeness it is necessary to consider the costs of the disclosure-based standard, the forgone benefits of the receipt-based standard, fully. If the receipt-based standard is unlikely to lead to greater information revelation, it could *prima facie* provide a greater deterrent against expropriation. Since the receipt-based standard is costlier than Part XI approval, the approval is likely to be the only process by means of which a controlling shareholder could ensure the immunity of a related party transaction. Assuming that the minority shareholders are unlikely to approve transactions that involve overreaching, such transactions would either not take place or if they do, they will proceed without the approval but carrying the risk of rescission indefinitely. The perpetual risk of the rescission then acts as a deterrent against the overreaching.

In contrast, the disclosure-based standard provides an avenue to immunise transactions by means other than the Part XI approval and therefore could lead to a deterrence deficit and hence to a greater level of expropriation. In addition, as was noted earlier, the deterrence is a function of monitoring as well as the rescission and it is possible that in the environment with a greater level of disclosure some shareholders would reduce their monitoring effort to examining the disclosed material only, so that some undisclosed transactions that would otherwise have been detected might be overlooked and hence unchallenged (Cheffins, 1997: 299; Ayres and Gertner, 1989: 106). In other words, the disclosure-based standard could lead to a reduction in monitoring and to this extent to the under-deterrence. Finally, under the disclosure-based standard claimants may have to demonstrate that they had no access to the

documents containing the disclosures to prevent the dismissal of their claims under the limitations statute. This increases the costs of seeking the rescission, reducing the probability that the rescission will be sought thus further eroding the deterrence of expropriation. The welfare gains from the disclosure would therefore have to be weighed against the welfare losses from the expropriation.

There are good reasons, however, to think that such losses are unlikely to be material and certainly not of such magnitude as to result in net welfare losses from the disclosure-based standard.

As to the possible under-deterrence due to a potential reduction in the monitoring, two factors indicate that the level of the minority shareholder monitoring is unlikely to differ under the disclosure-based or the receipt-based standard. If anything, it is more likely that more monitoring effort would take place under the disclosure-based standard. First, information-forcing rules, as Ayres and Gertner explain, are ‘more likely to be efficient if the private information is acquired passively’ (1989: 128).¹⁶ And this is the case with the minority outside shareholders. Such shareholders do not have the access to information that would reveal a related party transaction unless it is disclosed. They acquire the information passively, through press or whistleblowers etc, and consequently there is little scope to further dilute their incentives to monitor the undisclosed transactions. Indeed, the preceding section argued for a wholly different, contract-based, standard applicable to the shareholders who have access to the internal corporate records and who can therefore acquire the information actively. The important point for the present purposes is that since outside shareholders do not have the requisite access to information they are unable to acquire the knowledge of undisclosed transactions actively and hence are unable to improve on their monitoring effort whether under the disclosure-based or the receipt-based standard.

Secondly, with respect to the monitoring of the disclosed transactions it is likely that a greater level of monitoring would occur under the disclosure-based standard. The receipt-based standard can adversely affect the shareholders’ incentives to monitor the firms. Participation in general meetings, or otherwise making enquiries of suspect transactions, carry the risk that these actions will be used to establish evidence that the shareholder was put on notice for the purposes of article 181(2). To mitigate this risk, rational shareholders will respond by

¹⁶ Because there would be little effect on the parties’ private incentives to acquire the information themselves.

reducing, at least verifiable, monitoring effort.¹⁷ The disclosure-based standard, on the other hand, does not impose counter-productive incentives on the shareholders' monitoring in the same way the receipt-based standard does. On the contrary, the fact that disclosure could preclude claims filed after a year from the date the disclosure was made creates the incentive for shareholders to closely scrutinise the information the firms disclose.

As to the possible under-deterrence due to the unavailability of the perpetual rescission under the disclosure-based standard, it is important to appreciate that the standard does not simply replace the Part XI JSCA shareholder approval with the disclosure to shareholders. Under the standard, the fact of disclosure does not automatically immunise related party transactions. The shareholders would have a year from the date of disclosure to decide how to respond to the disclosed transaction: whether to demand that the transaction be approved at the general meeting;¹⁸ whether, and to what extent, to retain their shareholding or to 'exit' the firm; or whether to commence the section 84 action. The disclosure-based standard does not sanction expropriation.

On the contrary, if disclosed transactions raise shareholders' suspicions it is likely the transactions would be brought before a court. For this reason, it is doubtful that controllers would disclose transactions that involve overreaching in the first place. Overreaching is likely to be hidden and as such remain subject to the risk of rescission indefinitely.

Finally, as to the under-deterrence occasioned by the additional costs of having to show no access to the documentation containing the disclosure, in many instances the hurdle is likely to be insignificant. Shareholders would only need to show that they requested the annual or quarterly report and that their request was denied. In fact routine publication of these documents means that the issue will rarely arise in practice. Foreseeably the greater issue is likely to be whether the disclosure contained sufficient information to put shareholders on notice. But, on the one hand, the issue will be for the article 199(2) petitioner to establish and, on the other, it is just as likely to arise under the receipt-based standard as under the disclosure-based standard.

¹⁷ In other words the standard would make worse the already well documented collective action and free-rider problems.

¹⁸ Section 53(1) JSCA allows 2% shareholders to add items to the AGM agenda; section 55(1) JSCA allows 10% shareholders to demand an EGM.

Given these arguments, it is likely that the benefit of the potentially greater level of disclosure of transactions and conflicts occasioned by the disclosure-based standard would outweigh the welfare losses due to the departure from a more claimant friendly constructive knowledge standard. After all, information asymmetry is at the heart of the deterrence arguments for pro-investor rules (Cooter and Freedman, 1991: 1053, 1054) and in relation to the disclosed transactions, by definition, there is no asymmetry. The disclosure-based standard is arguably the welfare maximising standard for attributing knowledge to minority outside shareholders under the statute of limitations.

Avoidance of statute of limitations

In defence of applying the contract-based standard in cases brought by the controlling shareholders, it was argued above that such claimants should be subject to the same standard of knowledge attribution as the claimants in the company claims in order to sustain the welfare benefits of the standard in the latter category of cases. The problem with such application of article 181(2) is the ease with which the inside shareholders can avoid the statute by masquerading as minority shareholders: eg. by finding a sympathetic minority shareholder who would lend his name to the section 84 action or, even simpler, by holding a small part of the controlling stake via a separate entity and using that entity to litigate. Thus we saw from the case data examined in section 4.2.3 above that these practices take place in Russia and, indeed, the abnormal increase in the shareholder claims after 2002 was attributed precisely to the statute ‘avoidance’ cases.

The concluding section of Chapter 4 also outlined the difficulties for the courts in trying to curtail such practices by, for example, applying the contract-based standard to all the shareholder cases where a company pleads in support of the claimant. On the one hand, such doctrine is likely to prove ineffective at constraining the ostensible minority shareholder claims that are in fact brought by the controllers to overcome the companies’ limitation period. The company can strategically submit a manufactured defence stating that it opposes the shareholder’s action, hoping that the court will allow the shareholder’s action and rescind the transaction. On the other hand, and perhaps more importantly, the doctrine could prove detrimental to the minority shareholder claims. The company can strategically submit a manufactured claim stating that it supports the shareholder’s action, hoping that the court will assume the claim is being brought ostensibly by a minority shareholder to overcome the

companies' contract-based limitation period and dismiss the claim by applying the contract-based standard under article 181(2).

In other words, the combined effect of the contract-based standard of knowledge attribution in the company claims; the controlling shareholders' incentives to behave strategically; and the unverifiability of the controller's true motives in supporting the shareholder's claim creates an adverse selection problem for the courts: the difficulty in distinguishing between *bona fide* and ostensible minority shareholder claims in applying the article 181(2) statute of limitations where the claims are supported by the companies.

In the absence of the proper plaintiff and wrongdoer control principles in Russian jurisprudence, cases are brought before the arbitrazh courts by minority shareholders with companies making submissions in support of the shareholders' claims. Because of how the courts have construed article 181(2) in the company actions, such claims could fall into two categories: either the company supports the ostensible shareholder claimant to overcome the contract-based standard under the limitations statute that would otherwise apply were it to bring the claim itself; or, it supports a genuine minority shareholder claim to create an impression that the claim is only ostensibly brought by the shareholder to help the company overcome the statute of limitations, hoping that the court would dismiss the claim under the contract-based standard. Where a court can ascertain what type of claim is before it, it should apply the contract-based standard, which would dismiss the claim – otherwise the company would have brought the claim itself – in the former cases; and apply the disclosure-based standard in the latter cases. This, however, would be difficult for the court to accomplish because it cannot know the true motives behind the controllers' support for the minority action.

In these circumstances, the courts could opt to apply either the contract-based standard or the disclosure-based standard to all cases. Given that the contract-based standard will effectively preclude minority shareholder enforcement of Part XI JSCA and annihilate the incentives created by the disclosure-based standard – since the controlling shareholders would know that any challenge by a minority shareholder after one year from the transaction's completion can be stopped by the company's statement of claim in support of the shareholder, the need to

protect the transaction from potential challenges via disclosure seizures to exist – the courts should and, as shown below, do adopt the disclosure-based standard in such cases.¹⁹

However, exceptionally, there may be cases where the court is able to establish the true motives behind the company's support for the shareholder litigation and could therefore apply the contract-based standard without the risk of striking out a genuine minority claim. As will be seen from the case data, the FAC has applied the contract-based standard in some minority actions that are supported by companies but not the others. What distinguishes these cases is that some pre-action conduct by the companies' controllers revealed the avoidance of the statute as the true motive behind the support for the minority's claim. The prior conduct enabled the court to establish that the minority claim is ostensible and therefore to apply the contract-based standard with little risk of striking out *bona fide* minority action.

5.1.3 Hypothesis

The economic analysis above identified three possible constructive knowledge standards that the courts could apply in interpreting the article 181(2) statute of limitations in shareholder claims and suggested the circumstances in which a particular standard is likely to lead to efficiency gains. The analysis therefore makes possible to formulate a falsifiable judicial bias hypothesis against which the FAC jurisprudence can be tested as follows.

First, the analysis suggests that the contract-based standard provides the norm that is more likely to maximize the joint welfare of the parties if applied to the majority inside shareholders defined by reference to the 25 percent shareholding.

Second, in relation to the minority outside shareholders the disclosure-based standard is likely to be the optimal constructive knowledge norm. Of course, it is possible that in such cases the article 199(2) petitioners will be able to show evidence that would also support the more onerous receipt-based standard, for example, a claimant-shareholder's presence at the general meeting. However, in cases where the defendant cannot establish the evidence necessary for the receipt-based standard the courts should be able to dismiss claims provided

¹⁹ The outcome of this is that the benefits of contract-based standard – reduction in opportunism, incentives to improve internal control – are eliminated.

the evidence sufficient to discharge the disclosure-based standard is adduced.

Finally, in shareholder actions that are supported by the defendant companies, the courts ought to apply the disclosure-based standard unless they are able to ascertain that the minority action is ostensible (in reality a company action brought in the name of the shareholder to overcome the contract-based standard), in which case the contract-based standard should be applied to dismiss the claim under the statute.

The FAC jurisprudence inconsistent with the three postulates would support the judicial bias hypothesis.

5.1.4 Case data

The FAC dismissed 10 cases brought by shareholders on the basis of the article 181(2) statute of limitations. The cases represent 14 percent of all the shareholder cases where the court declined to invalidate the transactions. This contrasts sharply with the companies' litigation where the statute of limitation accounted for almost half (49 percent) of the judgments refusing claimants the invalidity of the transactions. Of itself the statistic suggests that the court has not construed the article 181(2) so as to impede shareholder enforcement of Part XI JSCA: had the FAC applied the contract-based standard to the minority shareholders, doubtless the figure would be considerably higher.

Furthermore, the FAC dismissed two cases on the basis of there being sufficient evidence to discharge the receipt-based standard. The defendants were able to demonstrate, in the first case,²⁰ that the claimant received all the relevant information concerning the transaction some two years prior to bringing the claim; and in the second case,²¹ that the claimant participated

²⁰ *Постановление ФАС Московского округа от 30.05.02 по делу N. КГ-А40/3309-02* CDN67. The court established that a letter concerning the challenged transaction, a loan assignment, was sent to and received by the claimant shareholder in July 1999. A copy of the contract, which disclosed that the two defendants had a common director, was enclosed with the letter. The minutes of the annual general meetings in 1999 and 2000 showed that the second defendant held in excess of 20% shareholding in the first defendant and that the transaction was not subject to approval at either of the general meetings. The claim was filed in January 2001.

²¹ *Постановление ФАС Московского округа от 27.07.04 по делу N. КГ-А40/6253-04* CDN127. The general meeting took place in June 2002, whereas the claim was filed in January 2004.

in a general meeting, which examined all the particulars of the transaction, some 18 months prior to bringing its claim.

Given the use of the receipt-based constructive knowledge standard no question of judicial bias should arise – the standard is congruent with the investor protection principle. Indeed, where there is sufficient evidence to discharge the receipt-based standard there is a high probability that the claimant had actual knowledge meaning that the absence of a prompt enforcement action upon discovery of the cause of action is more likely to indicate opportunism: contentment with the transaction's terms and its implications for the investors at the time the transaction is executed with the subsequent, delayed, rescission claim motivated by an agenda unconnected to protecting the minority shareholders' interests from expropriation.

This is clearly shown by the facts in *Постановление ФАС Московского округа от 27.07.04 по делу N. КГ-А40/6253-04* CDN127, one of the two cases dismissed under the receipt-based standard.

In this case, the challenged property sale was executed in October 2001, whereas the claim was only filed in January 2004. The FAC dismissed the claim on the ground that the claimant's director participated in a June 2002 general meeting held by the seller company, which approved the transaction. The court also established that the transaction did not involve a conflict of interest. Since there was a high probability that the claimant knew of the transaction, and there was no conflict of interest of which the meeting may not have been aware, the court dismissed the claim under article 181(2). Doubtless, the court could also have done so for no breach of Part XI JSCA.

Given these findings it is questionable why the claim was brought in the first place. Opportunism offers a credible explanation. In December 2003, less than a month prior to the filing of the claim in the instant case, the FAC for the Northern Caucasus circuit dismissed a rescission claim brought by the seller company alleging that the property sale violated the JSCA's substantial transactions approval rules.²² The court dismissed the claim because the claimant alleged that it was the purchaser company that violated the rules by not approving the transaction. The court held that the seller company was an inappropriate claimant because it was for the purchaser company and its shareholders to decide whether, and how, to

²² *Постановление ФАС Северо-Кавказского округа от 22.12.03 по делу N. Ф08-4352/2003.*

address the JSCA violations committed by its officers. Surely had there been any JSCA violations on the part of the seller company – the company brought the claim, its controllers would have had full access to evidence of any infringements – these would have been raised in the Northern Caucasus litigation, and would not have resulted in the filing of such an outlandish claim. For whatever reason the seller company and its shareholder brought their respective claims it is plain it had little to do with protecting the minority shareholders from harmful related party transactions.²³

The second claim dismissed under the receipt-based standard, *Постановление ФАК Московского округа от 30.05.02 по делу N. КГ-А40/3309-02* CDN67, however, involved a greater degree of knowledge inference because the shareholder, a corporate body, underwent a change of control before commencing the litigation and the FAC attributed the outgoing management's knowledge to the incoming liquidator. As will be explained below, such knowledge attribution gives rise to similar efficiency issues as the contemporaneous ownership rule discussed in section 5.2 below; and for this reason the consideration of whether economic efficiency offers a justification for the rule, so as to preclude inferences of judicial bias, will also be considered in that section. For the present purposes suffice it to observe that the judgment was delivered after the SAC issued its Decree No.18, which held that a change in the control of a juridical person does not affect its knowledge. This in itself is sufficient to dismiss the judicial bias hypothesis in relation to the case: the FAC was not interpreting incomplete legislation; it was applying the law in the manner stipulated by the SAC.

In the remaining eight cases – four brought by substantial shareholders and corporate insiders; four brought by minority shareholders – the FAC applied a constructive knowledge standard.

The next section considers the four cases in the former category. The claims were dismissed under the contract-based standard. The section demonstrates, first, that the substantial shareholders or corporate insiders brought the claims. This dismisses of the judicial bias

²³ The claimant shareholder was a majority (79.22%) shareholder in the seller company (at least on 30 July 2002). The seller company supported the shareholder's claim. The majority shareholder was bringing the claim, on this basis the court could also have dismissed the claim by calculating the limitation period from the date of the transaction had there been no evidence of actual knowledge. The shareholding data was taken from the www.lin.ru website, a database collating official disclosures made by firms registered in the Russian Federation. The relevant data was accessed at http://www.lin.ru/db/emitent/ECC563AF0AB1E988C3256D3B0047142D/section/owners/discl_org_digest.html . Accessed on 14 June 2011.

hypothesis in relation to the four cases. Second, the section shows that the facts of the cases strongly support the rationale for applying the contract-based standard to this category of claimants. The section that follows looks at the four minority shareholder cases. It demonstrates, first, that the FAC did not apply the disclosure-based standard and, to this extent, the four cases support the judicial bias hypothesis. Second, the section shows that the four judgments fall into the category where the controllers' prior conduct enabled the court to determine that the minority action was only ostensible and therefore, should not be treated as evidence of the judicial bias hypothesis. The section also examines the cases where the minority claimants were able to overcome the limitation statute, which suggests that the FAC applies the disclosure-based standard in such cases.

Insider cases

In four cases the FAC clearly applied the contract-based standard.²⁴ As stated above, the judgments would support the judicial bias hypothesis only if the minority outside shareholders brought the claims. Since, as shown below, the corporate insiders and substantial shareholders brought the claims, the judgments do not support the judicial bias hypothesis.

Thus, in *Постановление ФАС Московского округа от 21.03.03 по делу N. КГ-А40/382-03* CDN81 and *Постановление ФАС Московского округа от 01.12.05 по делу N. КГ-А40/11703-05* CDN151, the FAC applied the article 181(2) one-year limitation period calculated from the dates when the challenged transactions were completed but only after establishing that the claimants held substantial shareholding in the defendant firms at the time – 25 percent plus one share in the former case, and 26 percent in the latter. In reaching its conclusion in both cases, the FAC expressly held that JSCA provides the substantial shareholders with 'a real opportunity' to obtain all the relevant information concerning the firms' transactions and affairs. The court dismissed the claims upon establishing that, in the former case, the claimant offered no evidence to demonstrate that the defendant company had denied it, or otherwise obstructed, the access to corporate records; and in the latter case, that the details of the transaction were sent to all the shareholders ahead of the general meeting

²⁴ In *Постановление ФАС Московского округа от 01.12.05 по делу N. КГ-А40/11703-05* CDN151 disclosures concerning the transaction were made, so the case would have failed even on a less stricter standard, however the court held that it would have dismissed the case applying the limitation period from the date of the transaction's execution.

that approved the transaction – a clear evidence of no obstruction to the relevant corporate records.

In the remaining two cases the claimants did not have the requisite shareholding to qualify them as the majority or substantial shareholders. Other circumstances however, clearly brought the claimants within the category of corporate insiders despite their smaller shareholding: in both cases the claimants held posts with the defendant firms that granted them full access to the relevant corporate books and records. In *Постановление ФАС Московского округа от 09.07.03 по делу N. КГ-А40/4498-03* CDN88 the claimant, a 15 percent shareholder, served as the defendant's accountant during the period when the transaction was completed and, as the FAC established, had full access to the firm's internal documents showing its assets and transactions because all the records were prepared and maintained by the accounts department.²⁵ Similarly in *Постановление ФАС Московского округа от 08.12.03 по делу N. КГ-А40/9604-03* CDN106 the FAC established that the claimant shareholder was an employee of the defendant company responsible for the oversight of the asset sold pursuant to the challenged contract when the sale was completed. The four cases, therefore, do not support the judicial bias hypothesis.

What is more, the facts of these cases demonstrate the arguments offered above for applying the contract-based standard to corporate insiders and substantial shareholders, namely that their unrestricted access to corporate information indicates that their failure to challenge an apparently offending transaction within a year from it taking place is, at best, due to a deficient level of monitoring; and, at worst, due to opportunism – actual (albeit unverifiable) knowledge of full facts concerning the transaction from its completion; contentment with its terms and effects for the investors, which can be inferred from the absence of a prompt enforcement action; and a subsequent rescission claim motivated by an agenda unconnected to the terms of the transaction or its impact on minority shareholders.

In *Постановление ФАС Московского округа от 21.03.03 по делу N. КГ-А40/382-03* CDN81 Leadville Investments Ltd challenged the transaction between ZAO NTV-Plus and ZAO Bonum-1 – an agreement for Bonum to broadcast via its satellites NTV's programmes across Russia for a period of one-year – in August 2002, some 18 months after it was completed in January 2001. It argued, unsuccessfully, that it only discovered the existence of

²⁵ Additionally, the claimant's father and brother held 30% shareholding in the defendant firm.

the general meeting unapproved transactions between the two firms in an audit conducted in November 2001.

A number of factors cast doubt over the *bona fides* of the assertion. Leadville's claim was one of a number of cases involving Bonum, NTV, its majority shareholder Media Most and several of the group's, largely state controlled, creditors that began in May 1999 and were extensively reported by the media.²⁶ For example, in February 2001 press reports identified Bonum as NTV's subsidiary and that it was broadcasting NTV's programmes.²⁷ Had Leadville had a genuine concern with the terms of the broadcasting agreements, it could have made enquiries regarding any relevant approvals and, if necessary, judicially challenge their validity by January 2002.

Its failure to do so is best explained by factors other than its apparent lack of the relevant knowledge. In November 2001 Moscow's arbitrazh court placed Bonum-1 into involuntary administration.²⁸ It is likely that Leadville's claim was brought to escape NTV's liability under the contract and/or to leverage the NTV's bargaining position in the future settlement with Bonum's creditors²⁹ – not to protect NTV's minority shareholders from expropriation by the majority.

This is further supported by the fact that no expropriation of the minority shareholders was taking place. Bonum was NTV's wholly owned subsidiary. Transactions between the two firms would not have discriminated between NTV's shareholders. Furthermore, the contract price for the services was significantly below what other satellite firms charged NTV for the analogous services (and this was submitted by the claimant). It was clearly on terms advantageous to NTV and its shareholders.

In *Постановление ФАС Московского округа от 01.12.05 по делу N. КГ-А40/11703-05* CDN151 the claimant, OAO Rosneft, filed its claim against ZAO Rosshelf in February 2005 to rescind a transaction executed in September 2003 that was also approved as a substantial

²⁶ For a detailed discussion of the litigation involving Media Most and its subsidiaries see Pyanykh, 2001b.

²⁷ For example, in February 2001, in its coverage of the Bonum's, NTV's and RF Ministry of Finance litigation, Kommersant reported that Bonum was NTV's wholly owned subsidiary and that Bonum was broadcasting NTV's programmes. Surely during the whole of 2001 Leadville, reportedly a subsidiary of Gazprom-Media who was a major creditor of Media Most, as a 25 percent shareholder would have known that NTV held no general meetings to approve the transactions (Pyanykh, 2001a).

²⁸ Kommersant, 2001.

²⁹ The two firms settled within 3 months of the FAC's judgment. See Kommersant, 2003.

property transaction in an October 2003 extraordinary general meeting. It is highly unlikely that the delay in bringing the claim could be attributed to the lack of Rosneft's management's knowledge of the transaction or the alleged conflict of interest therein,³⁰ given the presence of the approval and the fact that all the transaction's details were sent to shareholders ahead of the general meeting.

The ultimately aborted merger between Gazprom and Rosneft announced in 2004 offers a better explanation. Pursuant to the RF Government's then plans, Rosneft was to be subsumed within Gazprom,³¹ with Rosneft's management becoming subordinate to Gazprom. The press widely reported that Rosneft was opposing the merger, prompting both companies to issue a joint press release – doubtless at the instigation of their political masters – stating that the companies 'had no conflicts of interest' (Chaika, 2005). The press release was issued on the 15th of February 2005. Rosneft filed its claim alleging Gazprom's conflict of interest in the Rosshelf transaction on 17 February 2005. In May 2005 the Government abandoned the merger.

In *Постановление ФАС Московского округа от 09.07.03 по делу N. КГ-А40/4498-03* CDN88 the claimant shareholder-accountant brought his challenge over four years following the transaction's completion. Again, the delay can be attributed to opportunism rather than the lack of the relevant knowledge: a conflict among the shareholders concerning the management of the two firms involved in the transaction, which erupted in 2002 shortly before the claim was brought. The court further established that both the seller and the buyer firms had identical shareholders, with identical proportions of their shareholding. This also indicates opportunism: irrespective of the transaction's terms, no shareholders were expropriated by the transaction.³²

³⁰ The court also held that the claimant failed to demonstrate that the transaction involved a conflict of interest. The transaction was a purchase of an unfinished gas pipeline by Rosshelf from OOO Transgascapital. Rosneft argued that OAO Gazprom had a conflicting interest as it held, together with its affiliates, 53% in Rosshelf and was itself carrying out completion works on the project. However, Rosneft did not offer any evidence, or indeed argue, that Gazprom had any affiliation with OOO Transgascapital. Lin.ru shows that Rosshelf's board called an EGM to approve the joint venture to develop the pipeline as a related party transaction. Rosneft did not challenge this, presumably because it was approved.

³¹ The RF Government would exchange its 100% holding in Rosneft for 11% of Gazprom (held by Gazprom's subsidiaries) thus giving the Government a controlling stake in Gazprom (Evplanov, 2004).

³² Indeed the claimant brought another claim challenging a sale of different property, shares in a third company, which the court dismissed on the ground that the claimant's rights were not affected. That case also established that the director who signed the sale purchase agreement was the claimant's

In *Постановление ФАС Московского округа от 08.12.03 по делу N. КГ-А40/9604-03* CDN106 the claimant shareholder-employee challenged the transaction executed in July 1999, almost four years after its completion, in June 2003. The reasons for the delay are unclear. However, the FAC established that the boards of both defendants approved the transaction prior to its completion. The claimant did not challenge this fact. Rather, his allegation was that the seller's board did not obtain an independent valuation of the transaction prior to granting the approval pursuant to section 77 JSCA. The section, as the court pointed out, only required such evaluation in the transactions involving a repurchase of shares, which was not the transaction that took place in the instant case. In other words, the case involved no breach of JSCA and the case could have been dismissed on this ground also. Given the absence of a breach it is doubtful the claim was concerned with minority shareholder protection.

Outsider cases

The final four cases the FAC dismissed under article 181(2) were brought by minority shareholders. As stated above, the judgments would support the judicial bias hypothesis if the court applied the contract-based standard or the disclosure-based standard but without examining whether the disclosures were made or whether they were made in a manner accessible to the minority shareholders – application of the disclosure-based standard without examining full facts of disclosure is tantamount to the contract-based standard because the court effectively assumes that the disclosure was made on the completion date or on the first reporting date following the transaction.

Prima facie the judgments support the judicial bias hypothesis. This is shown in the ensuing discussion of the facts of the four cases. However, as will be argued below, the four minority shareholder cases fall into the category of cases where prior conduct by the companies' controllers clearly indicates that the minority shareholders were ostensible – brought to help the firms overcome the limitation period set in the company claims. To support this claim it is further shown that in the minority shareholder cases that do not fall into this category, the court has applied the disclosure-based standard, reversing the lower courts' judgments that did not examine the full facts of the disclosure.

brother. That case could also have been dismissed under the statute of limitation, however it was not because the defendants did not plead the point as required by article 199. See *Постановление ФАС Московского округа от 03.09.03 по делу N. КГ-А40/6249-03* CDN93.

Two cases were brought by two separate shareholders against the same companies challenging the same contract, a sale of property.³³ The sale was executed in July 2002, whereas the claims were only filed in June and April 2005 respectively. In both cases the courts at all the instances held that the one-year limitation period commenced at the latest in 2003 because the documentation the firms were required to supply the shareholders with ahead of annual general meetings should have disclosed the transaction and the conflict of interest. In both cases, the courts rejected the submissions that the claimants' shareholding was below 25 percent – 0,008 and 22,38 percent respectively – which precluded their access to corporate books and records that contained all the relevant information. It also appears that the courts did not examine whether the relevant disclosures were in fact made to the shareholders ahead of the 2003 annual general meeting. To this extent the two judgments support the judicial bias hypothesis.

Two cases were brought by a group of shareholders against the same company challenging two separate property sales to two different purchasers.³⁴ Both contracts were executed in November 2000 but were only challenged in October and May 2003. The judgments do not disclose sufficient information to determine with certainty on what basis the courts attributed the relevant knowledge to conclude that the statute of limitations had passed: in one case the FAC held that the trial court correctly concluded that the claimants could have obtained all the relevant information by *bona fide* exercising their rights under the JSCA; in the other, the FAC stated that it concurred with the reasons given by the trial court in its conclusion on the statute of limitations point.³⁵ It might be speculated that had the relevant disclosures been made and accessible to the shareholders, the court would have highlighted that fact in its judgments. On this basis, the two judgments also appear to support the judicial bias hypothesis.

Nevertheless, it is submitted that the four judgments do not evince the judicial bias hypothesis for the following reasons. Thus, in both *Постановление ФАС Московского округа от 20.01.06 по делу N. КГ-А40/13482-05* CDN154 and *Постановление ФАС Московского округа от 26.01.06 по делу N. КГ-А40/13759-05* CDN155 the defendant company supported the shareholders' claims before the courts at all the three instances. On

³³ *Постановление ФАС Московского округа от 20.01.06 по делу N. КГ-А40/13482-05* CDN154; *Постановление ФАС Московского округа от 26.01.06 по делу N. КГ-А40/13759-05* CDN155.

³⁴ *Постановление ФАС Московского округа от 07.06.05 по делу N. КГ-А40/4554-05* CDN141; *Постановление ФАС Московского округа от 24.06.05 по делу N. КГ-А40/4653-05* CDN142.

³⁵ A search of the Moscow's AC case database did not reveal the judgments of the first instance court.

the basis of the above argument, the FAC could apply the statute of limitation to dismiss the claims as it did only if it could clearly ascertain that the company's conduct in the case was not intended to create an impression that the claim is only ostensibly brought by the shareholder to help the company overcome the statute of limitations, hoping that the court would dismiss the claim under the contract-based standard. In other words, if the court could establish that the shareholders' claims were in fact ostensible – brought to overcome the companies' statute of limitations – rather than 'made to look ostensible' by the actions of the company and its controllers.

The following facts demonstrate that the court could make that decision. By the time the shareholders filed their claims the two defendant companies were already involved in litigation over the disputed property.³⁶ This, prior, litigation was arguably sufficient for the court to determine that the shareholders' claims were in fact ostensible rather than 'made to look ostensible', that the shareholders' claims were company claims conducted by other means to overcome the contract-based standard.

There is a possibility, that the company's controllers foresaw the onset of the shareholder litigation and brought the claim purposefully to have it dismissed on the statute of limitation grounds, hoping that the dismissal of their claim may lead the courts to reject subsequent shareholder challenges to the transaction.

The possibility is likely remote. First, the litigation between the companies began with a claim to enforce the transaction, not to challenge its validity under section 84 JSCA. The company whose shareholders subsequently brought actions made a counter claim under section 84 in the enforcement proceedings. It was clearly trying to escape the transaction *ab initio*. Second, had the companies' litigation been used strategically to prejudice subsequent shareholder claims, it would have been started on suspicion that the shareholders have discovered the transaction. In both the shareholder cases however, the claimants stated that they only discovered the transaction from the litigation between the companies.

Other facts similarly indicate that the minority shareholder suits were company claims 'in disguise'. Another shareholder brought an identical claim in July 2005, which was not appealed after the first instance court dismissed the claim under article 181(2). In that case the court expressly held that the claim is being argued by the defendant company on behalf of

³⁶ Постановление ФАС Московского округа от 25.05.06 по делу N. КГ-А40/4607-06. The litigation started in May 2005, the shareholders brought their claims in April and June 2005.

the claimant, who did not appear at the hearings having made a written submission to consider the case in his absence and who did not provide any evidence to support his claim.³⁷ Had the company's support been nothing more than a smoke screen, it may be expected that the shareholder would have at least sought to appear before the court to raise this possibility.

Finally, the conflict of interest arose because the director of the transferor held twenty percent of the transferee's share capital. Members who collectively held seventy percent shareholding in the transferee brought a claim against the director seeking to exclude him from the transferee on the basis that he was obstructing the transferee's operations by refusing to complete the transfer of the disputed property in his position as a director of the transferor.³⁸ The claim puts it beyond doubt that the transferor company was supporting the shareholders' claims in a genuine opposition to the transfer rather than to thwart their chances of obtaining the rescission. This is sufficient to conclude that the shareholder cases were brought by corporate insiders albeit it appearing as minority shareholders. On this basis, the FAC was correct to apply the contract-based standard for the purposes of article 181(2). The cases therefore, do not support the judicial bias hypothesis.³⁹

In *Постановление ФАС Московского округа от 07.06.05 по делу N. КГ-А40/4554-05* CDN141 and *Постановление ФАС Московского округа от 24.06.05 по делу N. КГ-А40/4653-05* CDN142 the chronology of the events that took place prior to the shareholders' claims was as follows.

The transactions were executed in November 2000. In July 2001, upon a creditor's petition, the Moscow's Arbitrazh Court appointed a provisional administrator placing the transferor under observation, an insolvency procedure intended to preserve the debtor's assets.⁴⁰ In July 2002, the court replaced the provisional administrator with an external administrator.⁴¹ Upon

³⁷ *Постановление МАС по делу No. А40-42888/05-19-269.*

³⁸ *Постановление АСМО от 07.02.06 по делу No. А41-К1-18843/05.* Section 10 of the Limited Liability Companies Act 1998 permits members of LLCs who collectively hold 10% shareholding to apply to court to seek to exclude the member who grossly usurped his rights or responsibilities, or by his acts or omissions made the company's operations impossible or significantly obstructed them. The case was dismissed on the ground that the director could not be excluded from the transferee for his actions as a director of the transferor.

³⁹ In addition both cases were appealed to the Presidium of the SAC but the SAC Collegiate (three judges) did not allow the appeals to proceed to Presidium. See *Постановление Президиума ВАС РФ от 29.03.2006 No.2868/06* and *Постановление Президиума ВАС РФ от 19.04.2006 No.3600/06.*

⁴⁰ For an overview of the process see Oda, 2007: 215, 216.

⁴¹ For an overview see Oda, 2007: 218, 223.

appointment, the administrator brought a claim against the defendants in the (subsequent) shareholder cases seeking an order that the property (disputed in the shareholders' cases) be vacated so as not to obstruct the administration process. In March 2003, the FAC upheld the lower court's decision to refuse the order on the ground that the defendants disputed the debtor's title to the property and that therefore, the issue had to be resolved via a separate claim rather than by means of the interim injunctive relief sought by the administrator.⁴²

In April 2003, the administrator filed claims disputing the validity of contracts pursuant to which the properties were transferred.⁴³ Some 39 shareholders brought the first claim in May 2003. All but four withdrew their claims in the course of the proceedings.⁴⁴

As with the two shareholder cases discussed above, prior litigation between the defendant companies arguably enabled the court to determine that the shareholders' claims were ostensible: company claims that should have been pursued by the administrator but were conducted by the minority shareholders. The cases therefore, do not support the judicial bias hypothesis.

Additional evidence supports the argument that the four shareholder cases are exceptional in the sense described above so as to preclude inferences of judicial bias. First, there are minority shareholder cases that are supported by the defendant companies where the lower courts have sought, unsuccessfully, to apply the contract-based standard to attribute knowledge under article 181(2). The FAC reversed the judgments holding that the courts should have used the disclosure-based standard. What distinguishes these cases from the four discussed above is that there was no prior conduct, such as an earlier litigation, that would have enabled the court to determine that the companies' support of the claims was not premeditated to have the shareholders' claims dismissed under article 181(2).⁴⁵

Thus, in *Постановление ФАС Московского округа от 14.02.03 по делу N. КГ-А40/45-03* CDN94 the FAC sent the lower instance judgments for a retrial on the ground that their conclusions regarding the statute of limitation point were based on suppositions rather than

⁴² *Постановление ФАС Московского округа от 31.03.03 по делу N. КГ-А40/374-03.*

⁴³ Case numbers *A40-15707/03-68-154*; *A40-15710/03-45-149*; *A40-15715/03-40-154* registered with MAC on 18.04.2003.

⁴⁴ The May 2003 case was appealed to the Presidium of the SAC but the SAC collegiate (three judges) did not allow the appeals to proceed to presidium. *Постановление Президиума ВАС РФ от 14.10.2005 No.12407/06.*

⁴⁵ A search of the parties' names on the official court databases did not reveal any prior disputes concerning the disputed transactions.

case materials. In particular, the FAC held that the lower instance courts could not attribute the knowledge to the claimant on the ground that he should have discovered the disputed transaction and the circumstances indicating its invalidity at the general meeting that approved the annual report for the year when the transaction took place in the circumstances where neither the meeting's minutes, nor the relevant annual report were included in the case materials. Furthermore, the FAC stated that the courts failed to give full consideration to the submissions that the information concerning the transaction was only communicated to the shareholders in June 2002 (the sale was completed in October 1998); that the sale was not reflected in any of the company's annual reports; and that the shareholders had no access to the documents containing the information concerning the share sale.⁴⁶

Similarly in *Постановление ФАС Московского округа от 17.11.05 по делу N. КГ-А40/11191-05* CDN148 the FAC upheld the decision of the appellate court, which struck down the first instance court's judgment – the first instance concluded that the shareholder could access all the relevant material by exercising the rights under sections 89 and 91 JSCA – on the following grounds: the general meetings' minutes contained no information on the basis of which it could be concluded that the claimant knew of the transaction; the respondent did not provide a document disclosable under section 89 from which the claimant could discover the transaction's details; the claimant's shareholding was below 25 percent and therefore it had no access to the accounting books and records under section 91, and no evidence was provided that at any stage prior to bringing the claim the claimant held 25 percent of the defendant's share capital.⁴⁷

In conclusion it is apt to highlight that, as noted at the outset of this section, shareholder claims that fail under article 181(2) represent only 14 percent of the shareholder cases dismissed by the FAC. The majority of the shareholder cases were dismissed on other grounds, of which 77 percent (53 cases) relate to the application of the substantive rules (eg. failure to establish a section 81 conflict of interest; failure to establish a section 81 transaction; section 83 approval was obtained; failure to establish a breach of claimants' rights). Taking into account the judgments in favour of the shareholder-claimants, the

⁴⁶ Upon retrial the transaction was invalidated, *Постановление ФАС Московского округа от 03.09.03 по делу N. КГ-А41/6360-03* CDN94.

⁴⁷ For a similar judgment see also *Постановление ФАС Московского округа от 30.12.03 по делу N. КГ-А41/10363-03* CDN109. For analogous dicta in cases where the company did not support the shareholder see *Постановление ФАС Московского округа от 29.03.04 по делу N. КГ-А40/2053-04* CDN116; *Постановление ФАС Московского округа от 01.06.04 по делу N. КГ-А40/4080-04* CDN124.

number of the shareholder cases not barred by the statute of limitation is 70, which is 81 percent of all the cases brought by the shareholders within the case data.⁴⁸ It is fair to suggest that had the FAC used the contract-based standard to attribute knowledge in shareholder actions this figure would be *considerably* smaller.

5.2 Contemporaneous ownership rule

During the period surveyed in the thesis, the FAC dismissed six shareholder cases under the contemporaneous ownership rule. The rule requires claimants to establish that they were shareholders at the time when the disputed transaction was completed in order to bring the section 84 rescission claim. This section assesses whether the judgments support the judicial bias hypothesis. The section is structured as follows.

First, the section shows that the FAC began applying the rule prior to the emergence of the SAC jurisprudence on the issue. The FAC was filling a gap in the legislation and therefore its jurisprudence cannot be justified by reference to a higher legislative or judicial authority. Second, the section considers the literature that evaluates the contemporaneous ownership rule in Russia. It argues that the literature's explanation for the jurisprudence is incomplete. Third, the section addresses this gap in the literature. It offers a justification based on aggregate welfare maximisation, namely that the rule is necessary to enforce the information-forcing function of the disclosure-based standard for attributing the knowledge under article 181(2). Finally, the section examines the FAC's contemporaneous ownership rule jurisprudence. The case data suggests that the court's jurisprudence indeed reflects this rationale. For this reason, the section concludes that the judgments do not support the judicial bias hypothesis.

5.2.1 Analysis

The contemporaneous ownership rule is not legislatively defined in Russia (Gabov, 2005: 366; Telukina, 2005: 579).⁴⁹ In late 2003 – early 2004, the Presidium of the SAC applied the

⁴⁸ The figure does not include the judgments dismissed under the contemporaneous ownership rule because, as argued in the following section, the rule is closely related to the statute of limitation.

⁴⁹ Black et al, 2006b (English version: 53, Russian version: 65) attribute the rule to the SAC Decree No.19 of 18 November 2003 para.36. This is incorrect. Para. 36 only states that the statute of limitations is article 181(2). It contains no reference to the contemporaneous ownership rule. No

rule to reverse several lower courts' judgments that allowed shareholders to proceed under section 84 JSCA despite the fact that the claimants acquired their shares *ex post facto* the disputed transactions.⁵⁰ Three of the FAC's decisions applying the contemporaneous ownership rule were delivered prior to the emergence of the SAC doctrine.⁵¹ Even if the later FAC judgments can be justified by reference to the SAC doctrine, the FAC's prior jurisprudence cannot.⁵² In other words, the judgments require an explanation other than 'the FAC was applying the law as stipulated by the SAC' to dismiss the judicial bias hypothesis.

The SAC has justified the rule by reference to the rights and interests requirement discussed above: claimants' rights and legitimate interests cannot be infringed by a transaction completed prior to them acquiring the status of shareholders. The court offered two reasons for this conclusion. First, the right to bring a section 84 claim does not pass upon a transfer of title to a share; second, transactions that take place prior to the acquisition of shares cannot affect the economic interests of the claimants, in the sense that such claimants cannot be characterised as victims.⁵³

The reasoning is spurious and has been criticised in the literature. Even assuming that there may be a jurisprudential rationale why some shareholders' rights are transferable and others

other SAC Decrees known to the author refer to the rule. In contrast, the UK Companies Act 2006 section 260(4) expressly states that, for the purposes of the derivative suit, it 'is immaterial whether the cause of action arose before or after the person seeking to bring or continue the derivative claim became a member of the company'. Prior to the Act, the issue was undefined by the legislature or the courts (Law Commission, 1990: 109; Prentice, 1988: 62). The rule exists in a number of US State Corporate Statutes. Most notably section 327 of the Delaware General Corporation Law states 'In any derivative suit instituted by a stockholder of a corporation, it shall be averred in the complaint that the plaintiff was a stockholder of the corporation at the time of the transaction of which such stockholder complains or that such stockholder's stock thereafter devolved upon such stockholder by operation of law'. See Clark, 1986: 650-652.

⁵⁰ *Постановление Президиума ВАС РФ от 02.12.03 No.9736/03; Постановление Президиума ВАС РФ от 09.12.03 No.12258/03; Постановление Президиума ВАС РФ от 03.02.04 No.13732/03*; the earliest SAC judgment concerned the JSCA substantial transaction approval rules: *Постановление Президиума ВАС РФ от 21.10.03 No.10030/03*.

⁵¹ *Постановление ФАС Московского округа от 02.10.01 по делу N. КГ-А40/5398-01* CDN53, *Постановление ФАС Московского округа от 04.02.03 по делу N. КГ-А40/69-03* CDN79, *Постановление ФАС Московского округа от 30.06.03 по делу N. КГ-А40/4022-03* CDN87.

⁵² The SAC's subsequent adoption of the contemporaneous ownership rule is a factor indicating that the development of the rule in Russian jurisprudence was perhaps more of a general policy response than instances of judicial bias.

⁵³ See especially *Постановление Президиума ВАС РФ от 02.12.03 No. 9736/03; Постановление Президиума ВАС РФ от 09.12.03 No.12258/03*. See also Dobrovolskii, 2007: 47.

are not;⁵⁴ undoubtedly circumstances can arise where the shareholders' economic interests will be affected by the transactions completed prior to them acquiring that status. A common example, highlighted in the literature, is the lasting effect of transactions that can affect future profitability and dividend payments (Gabov, 2005: 369; Gureev, 2007: 128).

It is easy to foresee other examples where the shareholders' interests will be affected, which do not require the reliance on the 'lasting effect' argument. A person may purchase a share believing, on the basis of publicly available information, that the company holds good title to an asset only to discover subsequently that the asset has been sold to a related party. If the transaction was completed at an undervalue and was not reflected in the share price at the time the shares were acquired, the shareholder's economic interest will be tangibly affected the moment the financial market participants discover the transaction. The SAC's rights and interests justification for the rule seems unsatisfactory. It leads to further questions – What is the scope of the shareholders' rights and interests? Which rights can be transferred and how? – yet leaves them unanswered.

The difficulties with the SAC's reasoning, it is submitted, arise because the Russian doctrine does not characterise the section 84 rescission claim as a derivative action. If the courts were to conceptualise the claim as derivative the above questions would not arise: since the cause of action vests in the company, it is irrelevant whether the shareholder who brings the action on its behalf was a shareholder at the time the wrong was committed. However, if such reconceptualisation of the section 84 suit overcomes the jurisprudential questions that otherwise arise under the shareholders' rights and interests approach, it still calls for a justification of the contemporaneous ownership rule because the logic of the derivative action does not support it. Indeed, in jurisdictions such as Delaware where the shareholder enforcement of conflict of interest rules is founded upon the concept of derivative action, the imposition of the contemporaneous ownership rule has been criticised precisely for being illogical (Travis Laster, 2008: 676, 677). In the US and Delaware, policy reasons have been used to rationalise the existence of the rule namely, the prevention of the manufactured diversity of citizenship to gain access to the federal courts and the prevention of the purchased frivolous suits that are brought for their settlement value (Clark, 1986: 651; Travis Laster, 2008: 671 – 691).

⁵⁴ For example sections 89 and 90 grant shareholders access to financial information. The financial information is not limited only to the reports produced after a shareholder acquires shares in the company.

As shown below, the FAC's judgments can also be explained on a policy ground. The policy ground however, differs from those that have been used in the US and in the Russian literature to justify the contemporaneous ownership rule. The following discussion explains why the policy grounds are insufficient to justify the FAC jurisprudence so as to negate the judicial bias hypothesis and offers an alternative explanation.

Thus, manufactured diversity of jurisdiction has been identified as a problem in Russia and was expressly addressed by a 2009 amendment to the APC.⁵⁵ It is doubtful however, whether the prevention of the practice can explain the FAC judgments. The practice involves the purchasing of shares by a person in order to bring a suit in the judicial circuit where that person is located. It can only work successfully if the claimant's location determines the forum for the proceedings. Under the APC, the defendant's location determines forum.⁵⁶ Claimants can only choose between two competing forums; for example, where there are two defendants – as is the case in the section 84 rescission claims – located in different circuits. If this happens to be the case in a section 84 claim, the claimant's location remains irrelevant – the choice is limited to the two circuits where the defendants are located.⁵⁷

Second, assuming arbitrazh courts allowed the shareholders to proceed in the circuit where they are located in disregard of the APC, the practice may have been influential with the SAC but not with the Moscow's FAC for two reasons. First, as Russia's commercial centre Moscow has the largest concentration of companies in the country. It is likely that in many cases at least one of the defendants in a section 84 claim will be located in Moscow thus removing the need for a Moscow based would be claimant to purchase shares to bring the claim within the FAC's jurisdiction. Second, if the intention to create a diversity of jurisdiction is opportunistic it is unlikely that the Moscow FAC's circuit will serve that purpose. Opportunistic claims will work best in the judicial circuits where it is costly to put up a defence. Arguably, of the ten federal circuits in Russia, Moscow, as a commercial centre, will be one of the easiest circuits to defend proceedings.⁵⁸ Finally, to put the issue

⁵⁵ Administration of the Russian Federation, 2005: 9. Article 38(4.1) APC 2002 now requires all corporate litigation, including section 84 rescission claims, to be filed with Arbitrazh Courts where the company is located. Claimants in section 84 suits can no longer choose a forum where two arbitrazh courts have jurisdiction under article 36(7) APC 2002.

⁵⁶ Article 35 APC 2002; Article 25 APC 1995.

⁵⁷ Article 36(7) APC 2002; Article 26(1) APC 1995.

⁵⁸ See *Постановление ФАС Московского округа от 11.07.02 по делу N. КГ-А40/4393-02; Постановление ФАС Московского округа от 11.07.02 по делу N. КГ-А40/4394-02; Постановление ФАС Московского округа от 11.07.02 по делу N. КГ-А40/4395-02* where a

beyond doubt, all of the six FAC cases involved at least one defendant registered in the FAC's circuit – there was no need for a Moscow based claimant to bring the disputes within the FAC's jurisdiction.

It is also doubtful that the prevention of purchased frivolous suits can justify the FAC judgments. It is unlikely the contemporaneous ownership rule can bring about a sufficient reduction in opportunistic litigation to justify the likely reduction in the degree of investor protection. The case data examined in this thesis supports this conclusion. Even assuming that the six cases the FAC dismissed under the rule all involved frivolous litigants, they represent a small fraction of all the shareholder cases dismissed by the court. Indeed, in Delaware, the rule has been criticised precisely for being ineffectual at curbing opportunism, yet blunt and random in preventing potentially meritorious claims (Travis Laster, 2008). Thus, Clark, having considered the rationale for the contemporaneous ownership rule, observes as follows (Clark, 1986: 651):

'But it is easy, of course, to argue the opposing view.... If a person thinks he has a valid derivative claim against his corporation's directors and officers but is reluctant to start a lawsuit himself – perhaps because he lacks time or is risk-averse – it would appear to be a good thing, for himself and other shareholders, if he could sell his shares to a more daring investor who is willing to act as prosecutor on behalf of all the shareholders. Thus, it is difficult to justify the continued existence of the contemporaneous ownership rule.'

It follows from the above that the prevention of either the manufactured diversity of jurisdiction or the opportunistic litigation generally are unlikely to adequately justify the FAC's contemporaneous ownership rule jurisprudence. Other policy reasons appear to be necessary if one is to conclude that the jurisprudence does not evidence the judicial bias hypothesis.

Indeed, Russian commentary on the contemporaneous ownership rule has used a different rationale to explain the existence of the rule in the Russian jurisprudence. The rationale is the article 181(2) limitations statute. The commentary posits that the rule effectively acts as an

creditor tried to enforce guarantees against a group of companies whose shareholders challenged the validity of the guarantees in three different circuits in Russia. The bank argued that the companies could have challenged the validity of guarantees themselves as a counter claim in Moscow and that they were deliberately creating a diversity of jurisdiction using their shareholders located across Russia.

enforcement mechanism for the statute: without the contemporaneous ownership rule the statute would become indefinite.

The reasoning is straightforward. A claimant's acquisition of the relevant knowledge acts as the trigger for the statute. Since, it is argued, a claimant could not know of possible infringements of Part XI JSCA prior to becoming a shareholder, the statute cannot be triggered before the date when the claimant purchases the shares. It follows that every time a new shareholder purchases shares in a company, all its previous related party transactions will become reviewable under section 84 so that without the contemporaneous ownership rule, the statute of limitations would become defunct (Gureev, 2007: 128-130; Telukina, 2005: 579-581; Black et al 2006b, Russian version: 65).

It is submitted that the argument is acceptable but only up to a point. It is correct in focusing on the statute of limitations as the justification for the rule. The efficiency enhancing incentives created by the contract-based and disclosure-based standards of knowledge attribution under article 181(2), explained above, will disappear if the statute of limitations becomes defunct. A contemporaneous ownership rule is necessary to maintain those incentives. The argument, however, fails to take into account, on the one hand, the different standards of knowledge attribution under article 181(2). The failure leads to the assumption that non-shareholders cannot discover a company's related party transactions to enable knowledge attribution under article 181(2). This will be the case under the contract-based standard, which assumes that certain shareholders have superior access to corporate documents, or the receipt-based standard, which, if adhered to, would require evidence of direct receipt of the disclosure, to trigger the statute of limitations. Both standards require a claimant to be a shareholder before the limitation period can start running.⁵⁹ Under the disclosure-based standard the assumption does not necessarily hold. Rather, it depends on the manner in which the disclosure is made. If it is made in a document available to the public, such as the annual report for example,⁶⁰ then the relevant knowledge can be attributed to any person, shareholder or not.

On the other hand, the argument does not take into account that the statute of limitations cannot justify an *unqualified* contemporaneous ownership rule if it is to fulfil the efficiency criterion of aggregate welfare maximisation. The rule must operate on the same terms as the

⁵⁹ Of course, the receipt-based standard can apply to any one to whom the transaction is disclosed. The difficulty here is that the company would not know whom to disclose the transactions to.

⁶⁰ Section 92 JSCA; article 97 Civil Code.

statute. If it does not, the contemporaneous ownership rule will damage the efficiency enhancing incentives that the statute creates.

Thus, consider first the disclosure-based standard applicable to the minority shareholders. To recall, the standard operates as an information-forcing rule by placing the insiders that fail to make the requisite disclosure at a disadvantage to those that do: non-disclosed related party transactions carry the risk of invalidity indefinitely; disclosed related party transaction become immune after one year from the disclosure date. If the courts apply the contemporaneous ownership rule before the disclosure is made and, hence, before the statute is triggered for the existing minority shareholders, the rule will dilute the standard's information-forcing effect. This is because every time the minority shareholders trade their shares, the pool of claimants that can challenge undisclosed transaction shrinks.⁶¹ As the pool of claimants shrinks, the risk of indefinite challenge falls. The smaller the risk of indefinite challenge; the smaller the incentive to protect the transaction via disclosure.

The point can also be demonstrated by reference to the SAC Decree No.18 rule concerning the knowledge attribution for the purpose of article 181(2) to the shareholder-claimants who undergo a change of control prior to commencing litigation. Pursuant to the Decree No.18 a change in the shareholder's control does not affect its knowledge. It was noted in section 5.1.4 above that the interpretation of the rule may be explained under the same rationale as the contemporaneous ownership rule. Thus, since a shareholder's new management could not know of possible infringements of Part XI prior to assuming control, a company's related party transactions would become reviewable every time the control of at least one of its shareholders changes hands. In such cases, attribution of knowledge to the shareholder in a manner that disregards that the new management could not know of the transaction in effect operates as the contemporaneous ownership rule. However, the attribution of the outgoing management's knowledge to the new management requires that the outgoing management had knowledge of the transaction, actual or constructive, in the first place; because if they did not, there would be no knowledge to attribute to the new management.

If the claimant's shareholding is below 25 percent, then it can only be attributed knowledge under the disclosure-based standard: if the transaction was disclosed, the statute of limitations will expire in one year from the disclosure and the change of the shareholder's control will

⁶¹ The pool shrinks because 'new' shareholders buying shares entails that 'old' shareholders are selling the shares.

not affect this. But if no disclosure was made, so that the statute has not been triggered, the shareholder should be able to bring the claim despite its change of control. Decree No.18 states that a change of a juridical person's management does not affect its knowledge. If the shareholder has no knowledge prior to the change of control, this means that it also has no knowledge after the change of control for the purposes of article 181(2). Otherwise the statute of limitations will be triggered for a claimant-shareholder every time its control changes irrespective of the disclosure thus diluting the information-forcing function of the disclosure-based standard in the analogous way described in the preceding paragraph.

Indeed, in *Постановление ФАС Московского округа от 30.05.02 по делу N. КГ-А40/3309-02* CDN67 that was referred to in section 5.1.4 the court dismissed the shareholder's claim under article 181(2) but only after establishing that the disclosure was made. It is doubtful that the court could have dismissed the claim under article 181(2) had the disclosure not taken place. Arguably, the contemporaneous ownership rule, as in effect a functional equivalent of the standard for attributing knowledge to shareholders that undergo a change of control, should follow the same logic.

Put short, on the analysis above the date of disclosure of conflicts and transactions should be the operative provision that triggers the contemporaneous ownership rule rather than the date the transactions were executed. In the same vein, the non-disclosed transactions should remain judicially reviewable indefinitely irrespective of the time when claimants acquire their shares, subject only to two exceptions. The first relates to the claimants that acquire a 25 percent shareholding, or a smaller fraction that pushes their holding above the 25 percent threshold. In the preceding section it was argued that the contract-based knowledge standard is the welfare maximising article 181(2) interpretation in relation to such claimants. And in principle the contemporaneous ownership rule should operate in the analogous manner to the contract-based standard. The efficiency of the contract-based standard, however, is premised on the superior access to internal books and records that 25 percent shareholders enjoy under the JSCA, the access which they would not ordinarily have until the date the 25 percent holding is acquired. It follows that in respect of these claimants the contract-based standard should not apply to transactions executed prior to the acquisition of the threshold shareholding. Consistently with the economic rationale for the contract-based standard and article 181(2) such claimants should be able to challenge any non-disclosed transactions during the first year following the acquisition of their stake.

The second exception relates to the avoidance of the limitations statute, the issue discussed in some detail at the end of section 5.1.2 above. That discussion suggested that it would be relatively easy for the inside shareholders to circumnavigate the contract-based standard by finding minority shareholders who would lend their names to the section 84 action or by holding a small part of the controlling stake via a separate entity and using that entity to litigate. Perhaps it is easier still, and especially so for the insiders with a shorter foresight, to approach an acquaintance or to incorporate a new entity that would acquire shares in the company specifically to bring a lawsuit that would otherwise be time barred if the company was to issue proceedings itself. In such cases the courts ought to dismiss actions under the contemporaneous ownership rule.

Again, the difficulty here is the strategic behaviour by the controllers, which poses the risk for the courts of striking out a *bona fide* minority action. For this reason the discussion in section 5.1.2 concluded that the courts should adopt the disclosure-based standard in such cases unless the facts enable them to establish that the company's support for the shareholder litigation is not strategic to dismiss the action and could therefore apply the contract-based standard without the risk of striking out a genuine minority claim. The cases discussed in section 5.1.4 suggest that occasionally the courts are able to do so. Similarly with the contemporaneous ownership rule, the courts should apply it only where the article 181(2) period would have lapsed under the disclosure-based standard unless it is clear that the claimant is acting as a peg for the company to bring the proceedings outside the contract-based limitations statute standard.

5.2.2 Hypothesis

On the basis of the analysis above it is possible to formulate a falsifiable judicial bias hypothesis to test the FAC's contemporaneous ownership rule judgments that preceded the SAC jurisprudence on the subject. The FAC cases subsequent to the SAC jurisprudence, that is the cases decided after December 2003, do not support the judicial bias hypothesis because they accord with the superior legal authority. The analysis suggests that the efficiency of the contemporaneous ownership rule lays in its supporting function to the article 181(2) limitations statute. Thus, regarding the cases decided prior to December 2003, the FAC should not apply the rule indiscriminately to all the claimants that acquired their shareholding *ex post facto* the completion of transactions they seek to challenge. Rather the efficient

interpretation of the rule should be analogous to the judicial interpretation of the statute.

Hence, in cases where claimants acquire minority holdings *ex post facto* transactions the FAC should dismiss the claims under the contemporaneous ownership rule only if the article 181(2) limitation period would have expired under the disclosure-based standard for the existing shareholders. In other words, the rule should only apply where the proceedings are commenced one year after the disclosure of the transaction and conflict.

Where the statute of limitations has not expired under the disclosure-based standard, the FAC should apply the contemporaneous ownership rule only in two circumstances. First, where claimants who hold a 25 or a greater percentage shareholding bring proceedings after one year since the acquisition of their shareholding to rescind transactions completed prior to the date when the shareholding was acquired. Second, where the FAC is able to ascertain that the minority action is ostensible (in reality a company action brought in the name of the shareholder to overcome the contract-based standard), in which case the court should apply the contemporaneous ownership rule if one year from the completion of the transaction has passed.

The FAC's contemporaneous ownership rule jurisprudence consistent with the above propositions would not support the judicial bias hypothesis.

5.2.3 Case data

The six FAC judgments do not support the judicial bias hypothesis. The three judgments that predate the SAC contemporaneous ownership jurisprudence were decided in the manner consistent with the above welfare maximisation analysis. Indeed, the FAC cases decided after the SAC instantiated the blanket rule in Russian jurisprudence also display the circumstances that would have made the judgments inconsistent with the judicial bias hypothesis even in the absence of the SAC authorities. Finally, there is additional evidence of the FAC applying the rule consistently with the welfare maximization predictions in its judgments that struck down the lower courts' application of the contemporaneous ownership rule.

Thus, *Постановление ФАС Московского округа от 02.10.01 по делу N. КГ-А40/5398-01* CDN53 was the first FAC judgment to dismiss a shareholder's claim under the contemporaneous ownership rule. In December 1999 the defendant firms executed the disputed transaction, a supply of crude oil agreement. The claim was filed in May 2001. Although, the judgment does not disclose the claimant's shareholding or when it was acquired, the claimant did not dispute the fact that it was not a shareholder at the time of the transaction.

The FAC upheld the lower courts' reliance on the rule without discussing the grounds for its conclusion. Nevertheless, it is possible to conclude that the judgment does not support the judicial bias hypothesis – the statute of limitations would have expired under the disclosure-based standard by the time the proceedings were brought and, therefore, the FAC was correct to apply the contemporaneous ownership rule.

Thus, in March 1999 the seller's auditors issued a qualified audit statement in the annual report for the previous financial year announcing that in February 1999 the company received a letter from the president of the seller's holding company (the buyer) stating that from March 1999 the holding company will be responsible for its subsidiaries' export contracts which will be cleared by means of inter-group sale-purchase agreements. The opinion further stated that the draft agreements' crude oil prices were significantly below the world price of crude oil, which would jeopardise the company's ability to meet its current liabilities without attracting external funds and thus making it highly doubtful that the company could carry on as a going concern for the forthcoming year. The report was presented and discussed at the company's 1999 annual general meeting (Institute of Corporate Law and Governance, 2003: 23). In other words, related party transactions between the parent and the subsidiary were not hidden from the minority shareholders. The shareholders were put on notice for the purposes of the statute of limitations in 1999 so that by May 2001 the one-year period for bringing the section 84 suit would have expired.⁶²

In *Постановление ФАС Московского округа от 04.02.03 по делу N. КГ-А40/69-03* CDN79 the FAC expressly applied the contemporaneous ownership rule in conjunction with the disclosure-based standard under article 181(2). The disputed transaction was completed in July 1999 with the shareholder bringing its claim in July 2002. The court stated that not

⁶² The courts also established that the transactions were approved *ex post facto* at the 2001 general meeting.

only did the claimant held no shares in the defendant at the time of the transaction but also that the transaction was approved by the general meeting in May 2001, the fact which the claimant must have known both before and after acquiring its shareholding. Under the disclosure-based standard the statute of limitations would have expired before July 2002. In fact the statute would have expired even earlier since the claimant shareholder purchased its shares from the unsuccessful shareholder in *Постановление ФАС Московского округа от 30.05.02 по делу N. КГ-А40/3309-02* CDN67 and challenged the same transaction. The court applied the contemporaneous ownership rule in the manner consistent with the aggregate welfare maximisation criterion.

Finally, in *Постановление ФАС Московского округа от 30.06.03 по делу N. КГ-А40/4022-03* CDN87 the first instance court dismissed the shareholder's challenge, brought in September 2002, to a March 1998 agreement under the statute of limitations because the agreement's details were reflected in the 1999 – 2001 annual reports that were approved by the general meetings for the respective years. The shareholder appealed on the ground that she had no access to those documents because she only became a shareholder in December 2001. The appellate court dismissed her claim under the contemporaneous ownership rule. The FAC held that the courts at both instances correctly applied both the rule and the statute of limitations.

In fact the courts could have dismissed the claim irrespective of the disclosure because it was evident that the shareholder was acting as a peg for the company to issue proceedings to rescind the agreement. Pursuant to the agreement the company (an insurance provider) insured the second defendant (a bank) against default on loans to its customers. In late 2001, the bank's liquidator brought proceedings against the company to enforce the agreement. The company unsuccessfully sought to adjourn the proceedings on the ground that the agreement was being challenged in separate proceedings brought by its shareholder.⁶³ The rescission suit was clearly instigated by the company to circumvent the contract-based limitations statute, otherwise it could have simply counter-claimed in the enforcement proceedings brought by the bank. Indeed, when the shareholder failed before the appellate court, the company (not the shareholder) appealed to the FAC. Doubtless had its support for the shareholder was no more than a strategic attempt to dismiss the proceedings, that

⁶³ *Постановление ФАС Московского округа от 8.10.02 по делу N. КГ-А40/6680-02.*

objective would have been achieved at the appellate instance without a need to bring the case before the FAC.

The remaining three cases, *Постановление ФАС Московского округа от 14.04.04 по делу N. КГ-А40/2088-04* CDN118, *Постановление ФАС Московского округа от 26.04.04 по делу N. КГ-А41/2963-04* CDN120, and *Постановление ФАС Московского округа от 14.10.04 по делу N. КГ-А40/9131-04* CDN131 were decided after the contemporaneous ownership rule appeared in the SAC Presidium's jurisprudence. Nonetheless, the cases are worth mentioning.

The first two (unconnected) cases were remitted for retrial on the ground that the lower courts inadequately investigated the facts of both the claimants' shareholding at the time of the transactions *and* whether the statute of limitations had expired. In other words, the cases suggest that the statute of limitations is relevant to the application of the contemporaneous ownership rule.

In the third case, the court held that the appellate instance correctly established both that the statute of limitations had expired and that the shareholder did not have any shareholding in the first defendant at the time of the transaction. The judgment does not disclose on what basis the appellate instance reached its conclusion on the statute of limitations point. Although the contract was executed some time prior (June 1998) to the filing of the claim (November 2003) it is possible that no disclosures were made so that the statute would not have expired under the disclosure-based standard. However, the court could reach the decision irrespective of the disclosure. The facts made it plain that the company was pursuing the action using the shareholder to avoid the contract-based limitations statute. As with the case discussed above, when the shareholder failed before the appellate court, the company (not the shareholder) appealed to the FAC. Here too had its support for the shareholder was no more than a strategic attempt to dismiss the proceedings, that objective would have been achieved at the appellate instance without the need to bring the case before the FAC.

Finally, two further judgments, decided in the claimants' favour, demonstrate that the FAC's contemporaneous ownership rule jurisprudence is inconsistent with the judicial bias hypothesis: the court does not apply the rule in cases where the statute of limitations has not expired for the shareholders that held shares at the time of the transaction. The clearest example is *Постановление ФАС Московского округа от 14.07.03 по делу N. КГ-*

A41/4709-03 CDN89. In this case the FAC struck down the first instance judgment that applied the contemporaneous ownership rule stating that the court should have ascertained when the claimant learned or should have learned of the transaction rather than focusing on whether his rights could be affected given his lack of shareholding at the time the transaction took place. The FAC remitted the case for retrial directing the lower court to establish whether the company disclosed the conflict of interest for the statute of limitations purposes.

The second case, *Постановление ФАК Московского округа от 17.11.05 по делу N. КГ-А40/11191-05* CDN148 discussed in section 5.1.4 above, also offers some support for the proposition that in applying the contemporaneous ownership rule the FAC is more concerned with disclosure than with the timing of the shares acquisition, albeit indirectly. In this case, the claimant was a shareholder at the time of the transaction. However, its shares were sold after the transaction was completed but subsequently purchased again before the suit was brought. As explained above, the first instance court dismissed the claim under article 181(2). The court also held that the right to bring the section 84 suit was terminated when the shares were sold. The appellate instance decision, upheld by the FAC, stated that it was immaterial whether the shares were sold at some stage before the start of the proceedings: the only relevant facts were that the shareholder held shares at the time of the transaction and at the time when the claim was brought.

The judgment is difficult to reconcile with the rights and interests jurisprudence adopted by the SAC to justify the contemporaneous ownership rule. Its logic would support the first instance decision. A better explanation for the appellate and cassation judgments is the fact of non-disclosure of the transaction and the conflict of interest. The statute of limitations had not expired for the minority shareholders that held their shares when the transaction was completed. The buying and selling of shares by minority shareholders before the statute expires does not affect their right to enforce Part XI JSCA. In this case the courts could have reached the same conclusion even if the claimant held no shares at the time of the transaction.

Conclusion

This Chapter discussed certain procedural legislation relevant to the shareholder lawsuits under Part XI JSCA in Russia and appraised the FAC's application of those rules. The review of the case data suggests that the FAC procedural rules jurisprudence does not support the judicial bias hypothesis: the court has either applied the doctrine consistently with the

investor protection principle or deviated from it within the confines of the welfare maximisation or higher legal authority. Notably, the legislation offered some scope for the FAC to adopt stricter procedural rule interpretations – for example, by denying *locus standi* prior to the 2001 reforms or applying the contract-based standard for the purposes of article 181(2) to minority shareholders – and yet the court has not done so.

This is also supported by the descriptive statistics that can be derived from the case data. To be sure, the percentage of favourable decisions in the shareholder cases is smaller (20 percent) in comparison to the company cases (39 percent).⁶⁴ But the FAC's procedural rules doctrine is unlikely to account for these figures. Only 23 percent of unsuccessful shareholder suits failed on procedural grounds, in contrast to the 49 percent of unsuccessful lawsuits brought by companies.⁶⁵ In a significant majority of cases (81 percent) shareholders satisfy the procedural rules developed by the FAC.⁶⁶ And certainly there does not appear to be an analogous trend of the increasing use of procedural rules to curtail shareholder suits that was apparent in the companies' suits discussed in Chapter 3. These general observations as well as the specific case data discussed in this Chapter are difficult to reconcile with suggestion that the Russian judiciary was in some way lacking in its competence or impartiality.

The implications of the findings in this Chapter as well as the two Chapters that preceded it are considered next.

⁶⁴ 17 out of 86 and 33 out of 84 cases respectively.

⁶⁵ 16 out of 69 and 25 out of 51 cases respectively.

⁶⁶ 70 (17 cases decided in claimants' favour plus 53 decided against claimants on substantive grounds) out of the total 86 shareholder cases.

CHAPTER 6

CONCLUSION

Introduction

The FAC's procedural rule jurisprudence during the 1999 – 2006 period does not support the criticisms that the judicial institutional capacity in Russia was lacking for want of competence or honesty. The court applied the rules in congruence with the investor protection principle, aggregate welfare maximisation or higher order legal authority. These were the findings in Chapters 3 to 5. In this Chapter the discussion turns to consider generalisations and implications of the findings for the broader question posed at the outset of the thesis, namely what is the relationship between legal protection of investors ('on the books' and 'in action') and the development of stock markets in Russia and more generally. There are three distinct though not mutually exclusive possibilities: the protection is irrelevant; and/or detrimental; and/or facilitative to the market development. Each possibility is considered in turn.

6.1 Irrelevance

The irrelevance of the legal protection of investors to the development of equity markets becomes a possibility if one juxtaposes the thesis's finding that the judicial institutional capacity was not lacking with, at least the initial, failure of the Russian stock market to flourish. The implication is significant in that it contradicts the JSCA drafters' explanation for the failure of their self-enforcing law to bring about the sought after market outcomes (Black, Kraakman and Tarassova, 2000) and thus challenges the law matters thesis set out in Chapter 1.

Furthermore, whereas the principal arguments for the likely irrelevance of the investor friendly laws have here thereto been based on the positive observations of markets developing without the assistance of the law (Armour et al, 2009; Coffee, 2002; Cheffins, 2001), the findings add an example of a stock market failing notwithstanding the presence of the legal protections. Therefore, they make it harder to maintain that strong investor protection rules could still assume a positive role in stock markets development (even if the rules did not play a meaningful role in say the UK and US). And in doing so, the findings undermine claims to superiority of outside shareholder-oriented mandatory company law to the extent the normative appeal of such claims is based on the law matters thesis.

Admittedly, this rather negative implication for the law matters thesis has to be tempered by the limitations in the findings. Chapters 4 and 5 have demonstrated that the FAC did not bar the minority shareholder standing under Part XI JSCA either expressly or by a restrictive application of other procedural rules discussed in those Chapters. The Chapters, however, leave open the possibility that the court construed substantive rules, including the rights and interests requirement, in a manner prejudicial to the minority shareholders.¹

While a comprehensive review of the substantive rules jurisprudence was beyond the thesis's scope, it is possible to make some additional observations here in support of the proposition that strong investor protection law may be irrelevant to financial markets development. This could be achieved by narrowing down the review period to the time when the market was performing poorly and by focusing on the cases brought by shareholders.

Thus, Gorjaev and Zabotkin's analysis identifies October 2001 as the turning point in the Russian stock market development following which 'the most spectacular phase of the equity market's re-rating' occurred (2006: 389). This offers a fairly precise date as a marker to pinpoint the period when the Russian stock market experiment

¹ Of course, there is always a possibility that further empirical work, which was beyond the scope of this thesis, – for example, in addition to an examination of the FAC's substantive rules jurisprudence within the case data, a broader sample than the case data could survey jurisprudence of other federal and lower instance arbitrazh courts – could detract from the thesis's findings.

could have reasonably been considered a failure.² There are nine shareholder cases within the case data that were decided by the FAC up to and including October 2001. In two cases the FAC rescinded the challenged transactions.³ One case was dismissed on the ground that the transaction received the Part XI compliant approval *ex post facto* and was therefore valid. The case was discussed in Chapter 4 above.⁴ One case was dismissed under the contemporaneous ownership rule and was discussed in Chapter 5.⁵

The remaining five cases have not been dealt with in Chapters 4 and 5 and are therefore worth considering in more detail here. In four cases the claimants' failed to establish the presence of a section 81 JSCA conflict of interest. Three of the four cases contained no allegations of conflict of interest properly understood: the claimant-shareholders alleged that transactions were *ultra vires*. In these cases the shareholders sought to rely on the section 81 definition to argue that they themselves were 'interested' parties and could therefore bring actions for rescission under article 174 of the RF Civil Code, the operative provision for rescinding *ultra vires* transactions.⁶ In the fourth case the pleadings were made under Part XI JSCA properly understood, however, the pleaded conflict was fanciful: the alleged 'conflict of interest' arose because the director who executed the transaction pursuant to a power of attorney granted to him by the board was both a representative (because of the power of attorney) and director (by virtue of his membership of the board) of the company.⁷

² The period to October 2001 would include the period the JSCA drafters thought was a failure: their account of the Russian stock market experience was published in July 2000 (Black, Kraakman and Tarassova, 2000).

³ *Постановление ФАС Московского округа от 20.10.99 по делу N. КГ-А40/3359-99* CDN14; *Постановление ФАС Московского округа от 12.09.01 по делу N. КГ-А40/4892-01* CDN50.

⁴ *Постановление ФАС Московского округа от 19.05.99 по делу N. КГ-А40/1396-99* CDN5. See p.158 above.

⁵ *Постановление ФАС Московского округа от 02.10.01 по делу N. КГ-А40/5398-01* CDN53. See p. 212 above.

⁶ *Постановление ФАС Московского округа от 14.06.00 по делу N. КГ-А40/2221-00* CDN24; *Постановление ФАС Московского округа от 13.12.00 по делу N. КГ-А40/5551-00*, *Постановление ФАС Московского округа от 31.05.01 по делу N. КГ-А40/2625-01* CDN43; *Постановление ФАС Московского округа от 18.09.01 по делу N. КГ-А40/5058-01* CDN51.

⁷ *Постановление ФАС Московского округа от 18.09.00 по делу N. КГ-А40/4081-00* CDN35.

The fifth case was dismissed on the ground that the claimant shareholder failed to demonstrate a breach of its rights and interests.⁸ The case was the first FAC judgment to invoke the rights and interests jurisprudence and to do so as the sole ground to find against a claimant. The claimant, an open joint stock company, sought to rescind a sale of shares between another joint stock company, a bank (the defendant), and a purchaser also an open joint stock company that was joined to the proceedings as a third party. Several factors take the case outside the realm of a ‘conventional’ minority shareholder related party transaction dispute to the point that, even if considered in some way unfair, the case is scarcely demonstrative of the FAC failing to protect outside shareholder-investors from insider overreaching under the JSCA.

First, the defendant bank was subject to liquidation and made submissions in support of the claimant throughout the proceedings including before the FAC. In reality to the extent the dispute was at all concerned with asset diversion it would have been between the defendant’s creditors and the purchaser company. With the defendant in liquidation no value would likely have accrued to the shareholder-claimant from the relief sought. The appropriate claimant was the defendant who should have issued the proceedings itself. Secondly, the first instance court established at the outset that the share sale did not contravene section 77 JSCA, the provision, which at the time required the non-conflicted members of the board to establish market value of related party transactions. Notwithstanding its finding on section 77, the first instance court ruled in the claimant’s favour and rescinded the transaction under Part XI JSCA. Arguably, had there been any concerns regarding the transaction’s value these would have been highlighted in the judgment of the court, which after all was sympathetic to the claimant. This casts some doubt over whether the case was in fact concerned with expropriation.

Thirdly, the claimant shareholder was the issuer whose shares were sold pursuant to the transaction. It is therefore much more likely that its pursuit of litigation under Part XI was concerned with maintaining control over its shareholder body than with remedying expropriation. The genesis of the dispute further supports this conclusion.

⁸ *Постановление ФАК Московского округа от 09.11.00 по делу N. КГ-А40/5072-00, Постановление ФАК Московского округа от 05.06.01 по делу N. КГ-А40/2619-01* CDN44.

In March 1999, shortly after the share sale, the purchaser company sent a request to the claimant to amend its shareholder register to reflect the transfer. When the claimant refused the request, the purchaser complained to the Federal Commission on the Securities Markets, which investigated the complaint and concluded that the refusal was unfounded and hence contrary to the JSCA. Subsequently the purchaser obtained a court order pursuant to section 45(2.2) JSCA forcing the claimant to register the transfer. The FAC upheld the order in April 2000.⁹ Shortly after, in May 2000, the claimant issued the proceedings under Part XI JSCA.¹⁰ The case is arguably more an example of opportunistic insiders resisting change in the ownership of the company under their control than of insider overreaching of outside shareholder interests.¹¹

In sum, these shareholder cases appear to confirm that at least during the early period of the Russian stock market development, the period the JSCA drafters considered a failure in part due to defective legal institutions in Russia, the FAC did not construe the substantive JSCA anti-self-dealing protections of minority shareholders in the manner prejudicial to minority shareholders. The cases therefore add further support to the proposition that strong investor protection may be irrelevant to equity markets development.

There is one other possibility. The case data suggests that the FAC was not obstructive to minority shareholders during the early period. However, it does show a

⁹ *Постановление ФАК Московского округа от 03.04.00 по делу N. КГ-А40/3864-99*. The August 2001 amendments to the JSCA included a new provision that made it mandatory for joint stock companies with 50 or more shareholders to entrust compilation and maintenance of share registers to registrars licensed by the Federal Commission on the Securities Market (section 44(3.2) JSCA). For a discussion of the relevant rules, reforms, and problems with share register manipulation in Russia see Oda, 2007: 141-144.

¹⁰ Given that the claimant would have been on notice of the transaction since March 1999, the courts could have, and arguably should have, dismissed the claim under the article 181(2) statute of limitations. It would have been difficult for the claimant to argue lack of knowledge of the conflict because the conflict of interest was a straightforward common directorship in two open joint stock companies as opposing to some form of secreted affiliation.

¹¹ Events *ex post facto* the FAC decision also confirm the position. Within a month from the FAC judgment to uphold the share transfer, the liquidator sold the shares to a third party company and the claimant duly registered the transfer. This led to another round of litigation. The courts ordered the claimant to amend the register to restore the original transferee's rights on the ground that the liquidator and the claimant knew that they were acting contrary to the courts' orders in alienating and registering the shares. See *Постановление ФАК Московского округа от 29.04.02 по делу N. КГ-А40/2426-02*.

relative scarcity of shareholder actions, especially if one considers that the five section 84 actions discussed above perhaps should never have been brought by the shareholders. Generally, the nine shareholder cases within the first three years of the case data contrast sharply with 77 shareholder cases in the latter five years of the case data. This remains the case if, for the purpose of this exercise, one ignores the cases where the defendant companies supported the claimant shareholders: eight vs. 57 cases (an average of 2.7 vs. 11.4 cases per year).

It was suggested in Chapter 4 that the rise in shareholder litigation in the years after 2001, as apparent from the case data, was not disproportionate with the general increase in litigation before the FAC and that therefore it was not reflective of the then changes to the JSCA that put shareholder standing to sue under Part XI on the statutory footing. Nor was it indicative, it was argued, of a change in judicial attitudes to shareholder standing under the Part.¹² Yet, this finding still leaves open the possibility of suboptimal enforcement of Part XI JSCA during the early period, albeit occasioned by factors other than legal institutions. In other words, the data may in fact offer some support for a version of ‘law matters’ thesis if it shows that Part XI JSCA was under-enforced during the period leading up to October 2001 for whatever reason.

In fact, a range of reasons to be sceptical about the optimality of minority shareholder enforcement of Part XI JSCA was set out in Chapter 4.¹³ The reasons draw on theoretical understanding and experiences in jurisdictions other than Russia, including ‘the West’. What cases surveyed in this thesis add, and the four ‘no conflict’ judgments discussed above offer good examples, is that shareholders need some understanding of free market institutions and some sharing of the values of those institutions to be effective users of the legislation designed to safeguard those values and institutions. To paraphrase Professor Coffee, while stock markets may require ‘Western-style’ legislation and institutions to realise their full potential, Western-style legislation and institutions may require Western-style private actors to make full use of them (2001: 76, 77, 80 – 82). It may be unrealistic to expect such claimant constituency to emerge spontaneously in tandem with legislation, especially in a post-

¹² See p.p. 163 – 165 above.

¹³ See p.p. 136 – 140 above.

Soviet country that for 70 years was subject to a socialist rule and a system of beliefs abhorrent of free markets.

It is of course conceivable that a strong investor protection law, supported by a capable judiciary, may not be able to function in the vacuum and that to generate effective private enforcement the law would need ‘competent’ claimants to issue proceedings. However, it would be premature to characterise the early period story of the Russian stock market development as one of strong law ‘on the books’ and ‘in action’ laying dormant in wait for competent investor-litigators to emerge who then help the law and thereby the market realise their full potential. Claimants that could supply credible enforcement of Part XI JSCA existed, and as the case data indicates were active, during the early period.

Thus, in Chapter 3 it was suggested that the insolvency practitioners could provide a credible threat of the Part XI proceedings being instituted against the controlling shareholders.¹⁴ To be sure, under ordinary economic conditions insolvency may be too remote for most companies, and actions at the instance of insolvency practitioners may not generate sufficient litigation to result in the optimal level of enforcement.

The thesis has not sought to ascertain the optimal level of enforcement in Russia and for this reason it is not suggested that the insolvency practitioner enforcement was optimal. However, the 1998 financial crisis in Russia was arguably a cataclysmic event that took the economic conditions outside the bounds of the ordinary and thus ensured an unprecedented supply of the insolvency practitioner claimants. Furthermore, the case data analysis carried out in Chapter 3 shows that, save for exceptional cases, the FAC did not seek to constrain the insolvent claimants by means of the contract-based statute of limitations standard during the early period: the first ‘regular’ insolvent section 84 claims to be dismissed under the standard did not emerge until last quarter of 2002.¹⁵ An outcome of these legal and economic factors is that the FAC heard 22 section 84 cases brought by insolvency practitioners in the three years between 1999 and 2001; and decided 8 of these in the claimants’ favour. The 22 cases represent 39 per cent of all section 84 litigation before the court during

¹⁴ See p. 64 above.

¹⁵ See p.p. 108 – 117 above.

that period – arguably an improvement on the shareholder enforcement of Part XI JSCA at the time.

Of course, in the absence of some objective measure of the optimal level of private enforcement activity it is impossible to maintain that the insolvency practitioner litigation under Part XI JSCA ensured the optimal level of enforcement under the Part during the 1999 – 2001 period. It is therefore impossible to state conclusively that strong law on the books and in action supported by the optimal level of private enforcement failed to bring about the desired market outcomes and thus to rule out the law matters thesis.¹⁶ However, to the extent it is reasonably possible to generalise from the case data and from the ‘testing’ of the judicial bias hypothesis, the analysis carried out in this thesis indicates that at the time when the Russian stock market was considered at its weakest, the judicial institutional capacity was not deficient and there was an observable level of private enforcement activity. These findings support the proposition that strong investor protection may be irrelevant to equity markets development.

6.2 Detriment

A synthesis of generalisations and implications of the thesis’s findings for the question of the relationship between legal protection of investors and the development of the stock market in Russia ought to mention opportunism both by minority shareholders and insiders.

Some discussion of opportunistic litigation under Part XI JSCA by inside shareholders featured in all three core Chapters of the thesis. In Chapter 3 it was suggested that company suits under Part XI JSCA are brought for reasons that often have nothing, or little, to do with protecting the minority from insider overreaching, an observation confirmed by the case data.¹⁷ It was also suggested in that Chapter that the contract-based standard under the article 181(2) statute of limitations, the principal procedural rule used by the FAC to control litigation under Part XI, was

¹⁶ Arguably, until econometric analysis that quantifies optimality levels of the relevant private enforcement in Russia emerges, every study in this field would suffer from the same drawback.

¹⁷ See p.p. 65 – 67 and 122 – 131 above.

developed as a response to such opportunistic litigation.¹⁸ The case data in Chapters 4 and 5, however, indicates that the controllers can easily bypass the contract-based standard by bringing a claim in the name of a minority shareholder. It is evident from the case data that the FAC is suspicious of such claims, applying the contract-based standard in some cases. Yet, the court appears cautious not to apply the standard in every minority action that is supported by the company. And rightfully so, given the risk of the strategic litigation behaviour by the companies that could otherwise likely follow.¹⁹

Concerns with the minority shareholder enforcement of Part XI JSCA were outlined in Chapter 4. It was suggested that such lawsuits carry a risk of being brought contrary to the interests of the shareholders as a whole and that the purpose of procedural rules in company law is to reduce this risk by *inter alia* allocating litigation rights to persons who are capable to determine whether the litigation is in the interests of the company and its shareholders.²⁰ At the same time, it should be apparent that the disclosure-based article 181(2) standard and the contemporaneous ownership rule discussed in Chapter 5 leave great scope for opportunism. A shareholder with as little as one share in the company could bring the section 84 rescission action. Taken together with the low legal costs of bringing lawsuits it is not surprising that the minority shareholder opportunism has become a widely recognised problem in Russia.²¹ One former FAC judge summarised the problem as follows (Dobrovolskii, 2006: vii):

'The gaps in corporate legislation, as the arbitrazh practice shows, is often used by parties to abuse their rights. The courts are littered with claims to invalidate general meetings and transactions. The claimant, as a rule, has insignificant shareholding, his participation in the meeting could not influence the voting outcomes, and no losses were caused to the claimant.'

¹⁸ See p.p. 122 – 131 above.

¹⁹ See p.p. 163 – 167, 186 – 188, and 196 - 201 above.

²⁰ See p.p. 141 – 143 above.

²¹ For a monograph dedicated to the problem see Gololobov, 2004. Another study of related party transaction rules in Russia concludes, '[the rules] no longer seem to solve a problem, they have become a problem. As a result the institution of transactions involving a conflict of interest, has stopped playing its important role of regulating conflicts of interest and has become as a minimum the subject of barter and as a maximum the subject of corporate blackmail' Gabov, 2005: 382. See also Gureev, 2007: 119-140.

As was explained in Chapter 4 it was only in July 2009 that section 84 JSCA was amended to introduce measures intended to curb minority shareholder opportunism.²² None of these provisions existed throughout the period surveyed in this thesis. And it is an open question whether the policy makers' occupation with investor protection in Russia was responsible for the delay in bringing the legislation designed to curb opportunism. To what extent opportunism may have affected stock markets growth in Russia is difficult to estimate and similarly remains an open question. There are at least two reasons to be pessimistic however.

The first reason concerns the deterrence of overreaching, which as was explained in Chapter 2, may require the protection of harmless transactions as well as the rescission of unfair self-dealing.²³ The law and economics scholarship suggests that damage to harmless transactions at the hands of opportunistic litigants may reduce the insiders' incentives to forbear from expropriation, thus exacerbating the adverse selection problem in the equities market. In other words, the scholarship highlights subtleties in effecting the deterrence of undesirable conduct – and there is not an obvious reason for thinking that unfair self-dealing may be an exception. Clearly there is scope for empirical research to investigate whether and to what extent the predictions of economic models are reflected in the actual behaviour.²⁴ The models' predictions, however, are intuitive and Chancery judges in the UK (a country with a noticeably well-developed stock market) appear to have understood the benefits of rewarding honesty, as Chapter 2 sought to show.²⁵ The text of Part XI JSCA at the time of its enactment suggests that Russian policy makers were less intuitive.

The second reason concerns the protection of third parties particularly in the transactions involving shares of open joint stock companies. In Chapter 2 it was pointed out that where the investor protection principle conflicts with free transferability of shares rescission of transactions in pursuit of the former would

²² See p.p. 143, 144 above.

²³ See p.p. 36 – 40 above.

²⁴ Such a study would no doubt be difficult to carry out but perhaps not impossible. For example, it might be possible to review judgments rescinding ostensibly fair transactions and to then track the company through the press and online media to see whether there are further reports of expropriation.

²⁵ See in particular the discussion of *Boardman v. Phipps* [1967] 2 AC 46 at p.p. 39, 40 above.

undermine the latter and thus could turn out to the detriment of the stock market.²⁶ Cases examined in this thesis not only show that the problem is real but also that it is precisely cases of this nature that have marked a turning point in the FAC jurisprudence towards a less claimant friendly interpretation of the rules. *Постановление ФАС Московского округа от 12.01.00 по делу N. КГ-А40/4449-99* CDN20 discussed in Chapter 3 demonstrates the point well with respect to the development of the contract-based knowledge standard under article 181(2).²⁷ The same can be said regarding *Постановление ФАС Московского округа от 05.06.01 по делу N. КГ-А40/2619-01* CDN44 and the development of the rights and interests requirement discussed in section 6.1 above.

Of course the above provides an inadequate basis to maintain that the courts may have played a positive role in the growth of Russian equity markets by curbing opportunism. Empirical work examining the interaction between opportunism, legal norms enabling such behaviour and market outcomes has to emerge first. A crude measure suggests that such research would be worth pursuing: the early, 1999 – 2001, case data shows an overall success rate of 39 per cent in contrast to the 24.6 per cent in 2002 – 2006.²⁸

6.3 Facilitation

The generalisations and implications offered in the preceding two sections – that strong investor protection laws might have been irrelevant and perhaps even detrimental to the development of the Russian stock market – make a case for the law's facilitative role difficult. The decline in the claimants' success rate over the period when the market is considered to have performed relatively well in comparison to the earlier years further augments the difficulty. The difficulty, however, exists only in so far as strong investor protection laws are understood from the perspective described in this thesis as the orthodox approach to deterrence where 'strong minority protections respond to [the adverse selection] problem by reducing the risk of insider

²⁶ See p.p. 24 – 25 above.

²⁷ See p.p. 123 – 125 above.

²⁸ Between 1999 and 2001, 22 out of 56 cases were decided in favour of claimants; between 2001 and 2006, 28 out of 114 cases were decided in favour of claimants.

opportunism’ (Black, Kraakman, Tarassova, 1998: 25).²⁹ The difficulty can be overcome if one analytically sets aside the orthodox approach.

In Chapter 2 it was suggested that there might be a plausible alternative to the orthodox approach at least at the level of theory. The alternative posits that strong minority protections respond to adverse selection problem by incentivising insiders to reveal information rather than by reducing the risk of insider overreaching.³⁰ It was further argued in that Chapter that there was a real potential for such information-forcing rules to improve the level of information on related party transactions in the Russian market because of the otherwise deficient mandatory disclosure regime and the high direct and indirect costs of the Part XI JSCA approval process.³¹

On the basis of the analysis in Chapter 2, Chapter 5 argued that the FAC had developed two procedural rules – the disclosure-based article 181(2) knowledge standard and contemporaneous ownership rule – and applied them in the manner that created incentives for the insiders to disclose related party transactions. Crucially, the rules require legal grounds on which transactions can be held invalid and an effective judiciary to enforce those grounds. To this extent, the finding offers some support for the proposition that the development of financial markets requires strong investor protection laws on the books and in action, albeit it differs in the explanation of how strong laws and enforcement affect financial markets.

In this context the 2006 empirical study by Black et al is interesting (Black et al, 2006a). It finds an economically important and statistically strong relationship between governance and Russian firm’s market value. This suggests that those who compile the governance indexes can, at least to some extent, distinguish between ‘good’ and ‘bad’ companies. Furthermore, one of the study’s key findings is that certain indexes have a stronger correlation with the market values than others. One of the strongest sub-indexes in their study is Brunswick’s ‘asset transfers/transfer pricing’ (365, 378). It seems therefore, the analysts can distinguish firms that will and will not expropriate minority shareholders via related party transactions. Presumably, it would be difficult to compile the index that could have a statistically significant predictive value without observing the activity, which perhaps implies that the

²⁹ See p.p. 36 – 40 above.

³⁰ See p.p. 40, 41 above.

³¹ See p.p. 43 – 58 above.

activity is disclosed by some firms. Indeed, the study notes that since 1999 Russian governance has improved ‘substantially’ (364). It is cautious in drawing causal relationships, however speculates that improvements were voluntary (362), or were prompted by the desire to raise finance on international capital markets (364). It makes no reference to the role of law generally or to disclosure obligations more specifically, let alone the statute of limitations or contemporaneous ownership rule. Of course, the finding in Chapter 5 provides no basis to conclude that improved disclosure can be explained by the two rules. Yet, it suggests that it might, which could at least prompt further research.³²

Other empirical research to investigate the implications from findings in Chapter 5 is also conceivable. For example, in the leximetrics field a study could consider the interaction of legal and economic systems according to the law’s effect on information revelation rather than deterrence of overreaching. To make such a study meaningful deeper analysis of legal norms’ effect on information revelation will most likely be necessary. The discussion of deterrence in Chapter 2 and in the preceding section indicates that leximetric studies underpinning the law matters thesis may have adopted a too narrow concept of deterrence on the basis of which to code investor protection rules. The information-forcing function is also intuitive and may appear simple. But the simplicity is superficial, which should be evident from the discussion of literature relevant to the fairness review rule’s effect on information revelation in Chapter 2.³³ Indeed, that a statute of limitations might have an information-forcing effect while intuitive may not be immediately apparent to a company law scholar. In other words, the question of how law matters must be antecedent to the question of does law matter. As nearly two decades of academic debate about the law matters thesis show, that this should be so is not always intuitive.

³² For example, a survey of Russian firms that asked the management to rank the reasons for disclosing related party transactions.

³³ See p.p. 55 – 57 above.

APPENDICES

BIBLIOGRAPHY

APPENDIX 1

CONSULTANT+ AND OTHER STATISTICAL DATA

КонсультантПлюс - [Окно поиска]

Файл Правка Вид Сервис Окна Помощь О Компании

Меню Назад Увеличить шрифт

Карточка поиска Правовой навигатор Кодексы Справочная информация

Поиск в разделе: Судебная практика

Тематика
Вид документа
Принявший орган
Дата с 01.01.1999 по 31.12.2006
Номер
Суд первой инстанции
Надзор
Название документа
Текст документа
Когда получен
Папки документов

Найдено в разделе Судебная практика (поисковые поля: Дата)

- ☒ ФАС Волго-Вятского округа (20484)
- ☒ ФАС Восточно-Сибирского округа (33900)
- ☒ ФАС Дальневосточного округа (24961)
- ☒ ФАС Западно-Сибирского округа (48359)
- ☒ ФАС Московского округа (76559)
- ☒ ФАС Поволжского округа (38579)
- ☒ ФАС Северо-Западного округа (71025)
- ☒ ФАС Северо-Кавказского округа (25000)
- ☒ ФАС Уральского округа (61129)
- ☒ ФАС Центрального округа (32144)

Построить список

Помощь - F1

Найдено всего: 432140 документов

КонсультантПлюс - [Окно поиска]

Файл Правка Вид Сервис Окна Помощь О Компании

Меню Назад
Увеличить шрифт

Карточка поиска
Правовой навигатор
Кодексы
Справочная информация

Поиск в разделе: Судебная практика

Тематика
Вид документа
Принявший орган
Дата с 01.01.1999 по 31.12.2006
Номер
Суд первой инстанции
Надзор

Название документа
Текст документа "об акционерных обществах"
Когда получен
Папки документов

Найдено в разделе Судебная практика (поисковые поля: Дата, Текст докумен

☒ ФАС Волго-Вятского округа (616)
☒ ФАС Восточно-Сибирского округа (667)
☒ ФАС Дальневосточного округа (544)
☒ ФАС Западно-Сибирского округа (1035)
☒ ФАС Московского округа (2001)
☒ ФАС Поволжского округа (742)
☒ ФАС Северо-Западного округа (1038)
☒ ФАС Северо-Кавказского округа (680)
☒ ФАС Уральского округа (1297)
☒ ФАС Центрального округа (787)

Построить спл

Помощь - F1
Найдено всего: 9407 документов

Поиск по полю Текст документа

Основной поиск | Расширенный поиск |

Слова для поиска (вводите **полностью**):

81 или 82 или 83 или 84

Примеры: капитальный ремонт аренда
социальный вычет НДФЛ
входной НДС

Вводите слова с любыми окончаниями.

Для поиска слов, расположенных подряд, исп

Для поиска по началу слова используйте с

Подробное описание поиска

Для задания дополнительных параметров по

Судебная практика

- ✓ ФАС Волго-Вятского округа (219) из (616)
- ✓ ФАС Восточно-Сибирского округа (188) из (667)
- ✓ ФАС Дальневосточного округа (167) из (544)
- ✓ ФАС Западно-Сибирского округа (303) из (1035)
- ✓ ФАС Московского округа (491) из (2001)
- ✓ ФАС Поволжского округа (191) из (742)
- ✓ ФАС Северо-Западного округа (213) из (1038)
- ✓ ФАС Северо-Кавказского округа (204) из (680)
- ✓ ФАС Уральского округа (314) из (1297)
- ✓ ФАС Центрального округа (185) из (787)

Раздел Суд

ПОСТА
делу N
Конкурс
информ

ПОСТА
делу N
Исковы
собранны
наруше
провед

ПОСТА
делу N
В призн
имуще
законн

ПОСТА
делу N
Решени
правом
законн

ПОСТА
делу N
Решени
правом
законн

ПОСТА

Русский | English | Français

Телефоны справочной службы: +7 (495) 608 11 97, 608 11 94 Телефон доверия: +7 (495) 962-12-80

Полная версия | Карта сайта | Обратная связь



ВЫСШИЙ АРБИТРАЖНЫЙ СУД РОССИЙСКОЙ ФЕДЕРАЦИИ



О Высшем Арбитражном Суде РФ

Структура ВАС РФ

Правовые основы

Правовые позиции Президиума ВАС РФ

Примирительные процедуры. Медиация

Пресс-центр

Новости ВАС РФ

Выступления Председателя
Итоги работы арбитражных судов
Федеральные целевые программы

Пресс-релизы

Пресса о ВАС РФ

Пресса об арбитражных судах

Контакты

Научно-консультативный совет при ВАС РФ

Форум стран Азиатско-Тихоокеанского региона

Международное право и сотрудничество

Вестник ВАС РФ

Государственные закупки

АРБИТРАЖНАЯ СИСТЕМА РФ

Регламент АС РФ

ЗАСЕДАНИЯ ПЛЕНУМА И ПРЕЗИДИУМА ВАС РФ

2013
Июль 1
Август 2 3 4 5 6 7 8
Сентябрь 9 10 11 12 13 14 15
Октябрь 16 17 18 19 20 21 22
Ноябрь 23 24 25 26 27 28 29
30

● Будущие заседания
● Прошедшие заседания

Архив заседаний

График рассмотрения дел ВАС РФ в качестве суда первой инстанции

Подписка на новости



Translate this page
English
Microsoft® Translator

Постановления
Пленума ВАС РФ

Информационные
письма Президиума
ВАС РФ

Постановления
Президиума ВАС РФ

Проекты
документов
ВАС РФ

Онлайн-сервисы
Электронное правосудие

Главная страница | Пресс-центр | Новости ВАС РФ | Итоги работы арбитражных судов

Результаты работы арбитражных судов РФ в 1992-2001 годах

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Поступило исковых заявлений	479740	371755	284159	344348	394089	420609	493581	581729	634363	745626
из них:										
отказано в принятии, возвращено	130565	102730	77800	99899	92950	75721	74245	72729	66873	70561
Разрешено всего дел	338162	275304	208081	237291	290094	341537	398622	496739	539490	638287
в том числе:										
по спорам, возникающим из гражданских правоотношений	332716	264447	190471	213662	244467	258999	280583	286296	270499	298126
по спорам, возникающим из административных правоотношений	5446	10857	17610	23629	44272	80043	115108	203860	256740	315551
об установлении фактов, имеющих юридическое значение	-	-	-	-	129	226	303	624	1766	5617
о несостоятельности (банкротстве) (завершено производство)	-	74	231	716	1226	2269	2628	5959	10485	18993
Разрешено споров с нарушением срока	5553	9386	3207	3887	10340	13956	13107	19132	25057	29341
Разослано решений с нарушением срока	10561	10591	5804	7072	13341	14530	12824	15507	19317	21786
Обжаловано судебных актов в апелляционную инстанцию (кол-во дел)	19756	19002	17622	20289	38088	41398	46415	58530	67562	79957
Рассмотрено дел в апелляционной инстанции	19999	19143	17648	19612	25762	29304	33375	42822	50450	61464
из них: с нарушением срока	782	1697	524	514	2498	2953	3109	4447	6281	6968
Отменено, изменено судебных актов в апелляционной инстанции (кол-во дел)	3441	5317	5378	5812	7636	8977	9714	11940	13670	16436
Обжаловано судебных актов в кассационную инстанцию (кол-во дел)				2268	15918	21818	25583	34371	42828	55395
Рассмотрено кассационных жалоб федеральными арбитражными судами округов	-	-	-	1224	12084	16741	20274	27718	35732	47028
из них: с нарушением срока	-	-	-	-	256	194	239	369	396	545
Отменено, изменено судебных актов в кассационной инстанции (кол-во дел)	-	-	-	490	4884	6126	7209	9683	12252	14856
Обжаловано судебных актов в надзорном порядке (кол-во дел)	3602	8145	9312	11502	8587	10585	11809	13484	15797	18167
Рассмотрено заявлений принесении протестов	2963	7714	9207	11469	8355	9040	10332	11556	14494	16867
из них: принесено протестов	410	1954	2735	1835	759	673	565	487	584	570
Рассмотрено протестов	333	2021	2880	2137	715	859	680	549	606	566
из них: удовлетворено	272	1778	2566	1816	662	789	638	521	571	539
Вынесено частных определений	712	1542	1179	787	855	1496	1480	2280	1862	1466

МОЙ АРБИТР.
ПОДАЧА ДОКУМЕНТОВ В
АРБИТРАЖНЫЕ СУДЫ

КАРТОТЕКА
АРБИТРАЖНЫХ ДЕЛ

БАНК РЕШЕНИЙ
АРБИТРАЖНЫХ СУДОВ

КАЛЕНДАРЬ
СУДЕБНЫХ ЗАСЕДАНИЙ

МОБИЛЬНАЯ КАРТОТЕКА

ПОДАЧА ЖАЛОБ

Платежные системы
копировать

Обращения по судебным
делам

Презиум Online

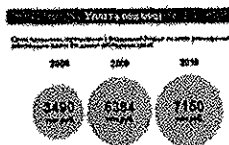


ПОИСК ПО САЙТУ

Решения по заявлениям
о признании нормативных
актов недействующими

Решения о назначении
арбитражным управлющим
наказания в виде
дисквалификации

СТАТИСТИЧЕСКИЕ ДАННЫЕ



Рассмотрено заявлений, связанных с исполнением судебных актов					13957	29367	42404	49329	49433	52633
Рассмотрено жалоб на постановления и действия судебных приставов-исполнителей							3680	8952	11123	11315
из них: признано обоснованными							1378	3576	4014	3709
Нагрузка на одного члена суда по разрешению дел и жалоб	27,9	20,8	14,9	17,5	19,6	21,6	23,9	28,1	29,6	34,2

© Высший Арбитражный Суд РФ

ТАБЛИЦА
ОСНОВНЫХ ПОКАЗАТЕЛЕЙ РАБОТЫ
АРБИТРАЖНЫХ СУДОВ РОССИЙСКОЙ ФЕДЕРАЦИИ
в 2002 - 2006 гг.

	2002	2003	± к 2002	2004	± к 2003	2005	± к 2004	2006	± к 2005
1	2	3	4	5	6	7	8	9	10
Поступило заявлений, исковых заявлений	854748	951778	+97030 (11,4%)	1340699	+388921 (40,9%)	1628133	+287434 (21,4%)	1080154	-547979 (33,7%)
<i>из них:</i>									
возвращено заявлений, исковых заявлений	72749 (8,5%)	62461 (6,6%)		69033 (5,1%)		79444 (4,9%)		82523 (7,6%)	
Рассмотрено дел в 1 инстанции	697085	869355	+172270 (24,7%)	1215627	+346272 (39,8%)	1467368	+251778 (20,7%)	1094849	-372519 (25,4%)
<i>в том числе:</i>									
по спорам, возникающим из гражданских правоотношений	317098	351640	+34542 (10,9%)	359863	+8223 (2,3%)	360812	+949 (0,3%)	372781	+11969 (3,3%)
по спорам, возникающим из админи- стративных правоотношений	325798	444804	+119006 (36,5%)	823236	+378432 (85,1%)	1080559	+257323 (31,3%)	654920	-425639 (39,4%)
о несостоятельности (банкротстве) (завершено производство)	44424	56440	+12016 (27,0%)	20116	-36324 (64,4%)	18812	-1304 (6,5%)	60848	+ в 3,2 раза
об установлении фактов, имеющих юридическое значение	9765	15424	+5659 (58,0%)	11016	-4408 (28,6%)	5538	-5478 (49,7%)	4523	-1015 (18,3%)
об оспаривании решений третейских судов и о выдаче исполнительных листов на принудительное исполне- ние решений третейских судов	672	936	+264 (39,3%)	1287	+351 (37,5%)	1593	+306 (23,8%)	1704	+111 (7,0%)
о признании и приведении в испол- нение решений иностранных судов и иностранных арбитражных решений	41	111	+70 (170,7%)	72	-39 (35,1%)	54	-18 (25,0%)	73	+19 (35,2%)

	2002	2003	± к 2002	2004	± к 2003	2005	± к 2004	2006	± к 2005
1	2	3	4	5	6	7	8	9	10
Рассмотрено дел в порядке упро- щенного производства	16139	67272	+51133 (316,8%)	175554	+108282 (160,9%)	188243	+12689 (7,2%)	73119	-115124 (61,2%)
Рассмотрено дел с участием ар- битражных заседателей	50	816	+766 в 16 раз	870	+54 (6,6%)	1115	+245 (28,2%)	953	-162 (14,5%)
Рассмотрено заявлений, жалоб, ходатайств	74793	122727	+47934 (64,1%)	166597	+43870 (35,7%)	174490	+7893 (4,7%)	198454	+23964 (13,7%)
из них:									
о применения обеспечительных мер	31084	45069	+13985 (45,0%)	53628	+8559 (19,0%)	48702	- 4926 (9,2%)	48954	+252 (0,5%)
в связи с совершением исполни- тельных действий	21013	24048	+3035 (14,4%)	25443	+1395 (5,8%)	26568	+1242 (4,9%)	30222	+3654 (13,8%)
в рамках дел о банкротстве	22696	53610	+30914 (136,2%)	87526	+33916 (63,3%)	99220	+11694 (13,4%)	119278	+20058 (20,2%)
Рассмотрено дел с нарушением срока	29899 (4,3%)	32565 (3,7%)		37348 (3,1%)		52351 (3,6%)		55602 (5,1%)	
Разослано решений с нарушени- ем срока	18982 (2,7%)	16777 (1,9%)		24447 (2,0%)		20740 (1,4%)		14693 (1,3%)	
Обжаловано судебных актов в апелляционную инстанцию (кол-во дел)	84984 (12,2%)	101729 (11,7%)		118245 (9,7%)		125882 (8,6%)		136626 (12,5%)	
Рассмотрено дел в апелляцион- ной инстанции	68769	84251	+15482 (22,5%)	100484	+16233 (19,3%)	109190	+8706 (8,7%)	115832	+6642 (6,1%)
из них:									
арбитражными апелляционными судами				6281		26824		41596	

	2002	2003	± к 2002	2004	± к 2003	2005	± к 2004	2006	± к 2005
1	2	3	4	5	6	7	8	9	10
Рассмотрено дел в апелляционной инстанции с нарушением срока	8868 (12,9%)	10534 (12,5%)		10330 (10,3%)		8139 (7,5%)		14363 (12,4%)	
Отменено, изменено судебных актов в апелляционной инстанции (кол-во дел)	18596 (2,7%)	21386 (2,5%)		22617 (1,9%)		25165 (1,7%)		24827 (2,3%)	
Обжаловано судебных актов в кассационную инстанцию (кол-во дел)	58719 (8,4%)	75274 (8,7%)		88679 (7,3%)		94511 (6,4%)		99109 (9,1%)	
Рассмотрено дел в кассационной инстанции	51022	64339	+13317 (26,1%)	77862	+13523 (21,0%)	83867	+6005 (7,7%)	87845	+3978 (4,7%)
из них: с нарушением срока	470 (0,9%)	723 (1,1%)		387 (0,5%)		566 (0,7%)		1795 (2,0%)	
Отменено, изменено судебных актов в кассационной инстанции (кол-во дел)	14939 (2,1%)	18720 (2,2%)		20656 (1,7%)		20748 (1,4%)		20667 (1,9%)	
Обжаловано судебных актов в порядке надзора (кол-во дел)	18043 (2,6%)	21830 (2,5%)		19935 (1,6%)		19472 (1,3%)		19460 (1,8%)	
Рассмотрено заявлений (представлений) о пересмотре судебных актов в порядке надзора	18500	15153	-3347 (18,1%)	15816	+663 (4,4%)	16172	+356 (2,3%)	16525	+353 (2,2%)
из них: передано дел в Президиум	417	239		224		379		296	
(% к количеству рассмотренных заявлений)	2,3%	1,6%		1,4%		2,3%		1,8%	
направлено дел в кассационную		246		135		240		164	

	2002	2003	± к 2002	2004	± к 2003	2005	± к 2004	2006	± к 2005
1	2	3	4	5	6	7	8	9	10
инстанцию (% к количеству рассмотренных заявлений)		1,6%		0,9%		1,5%		1,0%	
Рассмотрено дел Президиумом ВАС РФ	657	260	-397 (60,4%)	240	-20 (7,7%)	323	+83 (34,6%)	360	+37 (11,5%)
из них: отменены судебные акты (кол-во дел)	628	236		212		279		312	
(% к количеству дел, рассмотренных в первой инстанции)	0,09%	0,03%		0,02%		0,02%		0,03%	

Нагрузка на одного члена суда по рассмотрению дел и заявлений (средняя)	35,5	41,3		55,3		63,8		50,3	

Сумма госпошлины, перечислен- ная в федеральный бюджет по делам, рассмотренным арбитра- жными судами (млн.рублей)	975	1192		1474		1630		2035	

Контрольно-аналитическое управление
02.02.2007



РБА

среда, 14 июля 2010 г.

Итоги работы по рассмотрению дел

Сведения о количестве поступивших жалоб и обращений

Поиск по сайту >



[Главная](#) > [О суде](#) > [Итоги работы суда](#) > [Итоги работы по рассмотрению дел](#)

Итоги работы по рассмотрению дел

Динамика рассмотрения дел в ФАС МО.

Поступило в ФАС МО кассационных жалоб:

Год	Количество касс. жалоб
1996	2 404
1997	2 851
1998	3 841
1999	5 126
2000	7 190
2001	9 374
2002	10 111
2003	12 541
2004	14 314
2005	15 524
2006	15 141
2007	16 343
2008	14 989
2009	17 012

Рассмотрено дел в ФАС МО:

Год	Количество дел
1996	1 902
1997	2 254
1998	3 047
1999	4 185
2000	6 001
2001	7 816
2002	8 852
2003	11 051
2004	12 867
2005	13 360
2006	13 493
2007	14 233
2008	13 292
2009	14 892

Отменено судебных актов ФАС МО надзорной инстанцией:

Год	Количество судебных актов
1997	90
1998	85
1999	78
2000	81
2001	80
2002	120
2003	52
2004	51

Банк решений арбитражных судов

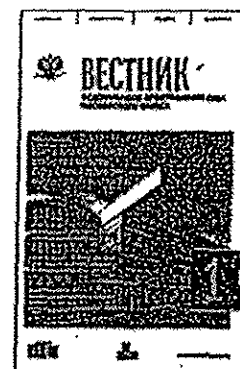
Калькулятор расчета процентов по ст. 395 ГК РФ

Телефонный справочник

Подписка на новости и информацию о деле

Судебные органы. Органы власти

Система подачи жалоб



2005	49	Итоги работы Федерального арбитражного суда Московского округа в 2005 году
2006	73	Итоги работы Федерального арбитражного суда Московского округа в 2006 году
2007	65	Итоги работы Федерального арбитражного суда Московского округа в 2007 году
2008	65	Итоги работы Федерального арбитражного суда Московского округа в 2008 году
2009	87	Итоги работы Федерального арбитражного суда Московского округа в 2009 году

Также в разделе:

- Информация об итогах работы Федерального Арбитражного суда Московского округа в 2009 году из доклада Председателя суда Адамовой В.Б. на состоявшемся 5 февраля расширенном заседании Президиума, посвященном подведению итогов работы суда в 2009 году.
- Итоги работы Федерального арбитражного суда Московского округа в 2008 г.
- Итоги работы Федерального арбитражного суда Московского округа в 2007 году.
- Итоги работы Федерального арбитражного суда Московского округа в 2006 году.
- Итоги работы Федерального арбитражного суда Московского округа в 2005 году.
- Итоги работы Федерального арбитражного суда Московского округа в 2004 году.
- Итоги работы Федерального арбитражного суда Московского округа в 2003 году.

© Федеральный арбитражный суд Московского округа
© Разработка: "Гарант-Интернет"

APPENDIX 2

CASE DATA

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S.84 JSCA invalidity (last known outcome)	Grounds	Observations
1.	<i>Постановление ФАС Московского округа от 9.02.99 по делу N. КГ-А40/46-99</i>	COY	Retrial: Refusal reversed	Part XI JSCA compliance not examined by lower courts	Insolvency claim
2.	<i>Постановление ФАС Московского округа от 31.03.99 по делу N. КГ-А40/772-99</i>	COY	Granted	Part XI JSCA breach	
3.	<i>Постановление ФАС Московского округа от 13.04.99 по делу N. КГ-А40/917-99</i>	COY	Granted	Part XI JSCA breach	
4.	<i>Постановление ФАС Московского округа от 5.05.99 по делу N. КГ-А40/1166-99</i>	COY	Granted	Part XI JSCA breach	
5.	<i>Постановление ФАС Московского округа от 19.05.99 по делу N. КГ-А40/1396-99</i>	SHR	Refused	Section 83 approval obtained	
6.	<i>Постановление ФАС Московского округа от 07.07.99 по делу N. КГ-А40/2002-99</i>	COY	Refused	Section 81 conflict not established	
7.	<i>Постановление ФАС Московского округа от 26.07.99 по делу N. КГ-А40/2274-99</i>	COY	Retrial: Refusal reversed	Presence of Part XI JSCA conflict insufficiently examined by lower courts	
8.	<i>Постановление ФАС Московского округа от 03.08.99 по делу N. КГ-А40/2331-99</i>	COY	Refused	Section 81 conflict not established	

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S.84 JSCA invalidity (last known outcome)	Grounds	Observations
9.	<i>Постановление ФАС Московского округа от 4.08.99 по делу N. КГ-А40/2383-99</i>	COY	Granted	Part XI JSCA breach	
10.	<i>Постановление ФАС Московского округа от 4.08.99 по делу N. КГ-А40/2531-99</i>	COY	Granted	Part XI JSCA breach	
11.	<i>Постановление ФАС Московского округа от 16.08.99 по делу N. КГ-А40/2560-99</i>	COY	Granted	Part XI JSCA breach	
12.	<i>Постановление ФАС Московского округа от 24.08.99 по делу N. КГ-А40/2657-99</i>	COY	Granted	Part XI JSCA breach	Insolvency claim
13.	<i>Постановление ФАС Московского округа от 19.10.99 по делу N. КГ-А40/3371-99</i>	COY	Refused	Section 83 approval obtained	Insolvency claim
14.	<i>Постановление ФАС Московского округа от 20.10.99 по делу N. КГ-А40/3359-99</i>	SHR	Granted	Part XI JSCA breach	
15.	<i>Постановление ФАС Московского округа от 27.10.99 по делу N. КГ-А40/3480-99</i>	COY	Granted	Part XI JSCA breach	Insolvency claim
16.	<i>Постановление ФАС Московского округа от 27.10.99 по делу N. КГ-А40/3503-99</i>	COY	Refused	Statute of limitations	Insolvency claim
17.	<i>Постановление ФАС Московского округа от 16.11.99 по делу N. КГ-А41/3737-99</i>	COY	Refused	Section 83 approval obtained	Insolvency claim

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S 84 JSCA invalidity (last known outcome)	Grounds	Observations
18.	<i>Постановление ФАС Московского округа от 7.05.99 по делу N. КГ-А40/1257-99; Постановление ФАС Московского округа от 22.12.99 по делу N. КГ-А40/4212-99</i>	COY	Granted	Non- Part XI JSCA grounds (Part XI JSCA not argued on second appeal)	
19.	<i>Постановление ФАС Московского округа от 29.12.99 по делу N. КГ-А41/4350-99</i>	COY	Granted	Part XI JSCA breach	
20.	<i>Постановление ФАС Московского округа от 12.01.00 по делу N. КГ-А40/4449-99</i>	COY	Refused	Statute of limitations	
21.	<i>Постановление ФАС Московского округа от 14.10.99 по делу N. КГ-А40/3337-99; Постановление ФАС Московского округа от 07.03.00 по делу N. КГ-А40/739-00</i>	COY	Refused	Section 81 transaction not established	Insolvency claim
22.	<i>Постановление ФАС Московского округа от 29.09.99 по делу N. КГ-А40/3117-99; Постановление ФАС Московского округа от 29.09.99 по делу N. КГ-А40/3135-99; Постановление ФАС Московского округа от 18.04.00 по делу N. КГ-А40/1376-00</i>	COY	Refused	Section 81 transaction not established	
23.	<i>Постановление ФАС Московского округа от 31.05.00 по делу N. КГ-А40/2120-00</i>	COY	Refused	Section 83 approval obtained	Insolvency claim

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S.84 JSCA invalidity (last known outcome)	Grounds	Observations
24.	<i>Постановление ФАС Московского округа от 14.06.00 по делу N. КГ-А40/2221-00</i>	SHR	Refused	Section 81 conflict not established	
25.	<i>Постановление ФАС Московского округа от 26.06.00 по делу N. КГ-А41/2481-00</i>	COY	Granted	Part XI JSCA breach	
26.	<i>Постановление ФАС Московского округа от 05.07.00 по делу N. КА-А41/2780-00</i>	COY	Refused	Section 83 approval obtained	Insolvency claim
27.	<i>Постановление ФАС Московского округа от 10.07.00 по делу N. КГ-А40/2781-00</i>	COY	Retrial: Refusal reversed	Presence of Part XI JSCA approval insufficiently examined by lower courts	Insolvency claim
28.	<i>Постановление ФАС Московского округа от 26.07.00 по делу N. КГ-А41/3112-00</i>	COY	Retrial: Refusal reversed	Presence of Part XI JSCA approval insufficiently examined by lower courts	Insolvency claim
29.	<i>Постановление ФАС Московского округа от 31.07.00 по делу N. КГ-А41/3145-00</i>	COY	Refused	Section 83 approval obtained	Insolvency claim
30.	<i>Постановление ФАС Московского округа от 4.08.00 по делу N. КГ-А40/3318-00</i>	COY	Retrial: Refusal reversed	Lower courts insufficiently investigated claimant's knowledge under statute of limitations	
31.	<i>Постановление ФАС Московского округа от 07.08.00 по делу N. КГ-А41/3285-00</i>	COY	Retrial: Refusal reversed	Presence of Part XI JSCA approval insufficiently examined by lower courts	Insolvency claim

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S.84 JSCA invalidity (last known outcome)	Grounds	Observations
32.	<i>Постановление ФАС Московского округа от 07.08.00 по делу N. КА-А41/3338-00</i>	COY	Refused	Section 83 approval obtained	Insolvency claim
33.	<i>Постановление ФАС Московского округа от 07.08.00 по делу N. КА-А41/3356-00</i>	COY	Refused	Section 83 approval obtained	Insolvency claim
34.	<i>Постановление ФАС Московского округа от 09.08.00 по делу N. КГ-А41/3341-00</i>	COY	Refused	Section 83 approval obtained	Insolvency claim
35.	<i>Постановление ФАС Московского округа от 18.09.00 по делу N. КГ-А40/4081-00</i>	SHR	Refused	Section 81 conflict not established	
36.	<i>Постановление ФАС Московского округа от 28.09.00 по делу N. КГ-А40/4346-00</i>	COY	Refused	Section 81 conflict not established; Section 81 transaction not established	
37.	<i>Постановление ФАС Московского округа от 22.01.01 по делу N. КГ-А40/6329-00</i>	COY	Granted	Part XI JSCA breach	Insolvency claim
38.	<i>Постановление ФАС Московского округа от 8.02.01 по делу N. КГ-А41/114-01</i>	COY	Refused	Statute of limitations	
39.	<i>Постановление ФАС Московского округа от 5.03.01 по делу N. КГ-А41/708-01</i>	COY	Refused	Statute of limitations	
40.	<i>Постановление ФАС Московского округа от 16.04.01 по делу N. КГ-А40/1653-01</i>	COY	Granted	Part XI JSCA breach	

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S.84 JSCA invalidity (last known outcome)	Grounds	Observations
41.	<i>Постановление ФАС Московского округа от 11.10.00 по делу N. КГ-А40/4591-00; Постановление ФАС Московского округа от 18.04.01 по делу N. КГ-А40/1673-01</i>	COY	Refused	Statute of limitations	
42.	<i>Постановление ФАС Московского округа от 24.05.01 по делу N. КГ-А40/2518-01</i>	COY	Granted	Part XI JSCA breach	Insolvency claim
43.	<i>Постановление ФАС Московского округа от 13.12.00 по делу N. КГ-А40/5551-00; Постановление ФАС Московского округа от 31.05.01 по делу N. КГ-А40/2625-01</i>	SHR	Refused	Section 81 conflict not established; Breach of claimant's rights not established	D1 supports claim
44.	<i>Постановление ФАС Московского округа от 09.11.00 по делу N. КГ-А40/5072-00; Постановление ФАС Московского округа от 05.06.01 по делу N. КГ-А40/2619-01</i>	SHR	Refused	Breach of claimant's rights not established	D1 supports claim
45.	<i>Постановление ФАС Московского округа от 16.04.01 по делу N. КГ-А40/1653-01; Постановление ФАС Московского округа от 24.07.01 по делу N. КГ-А40/3779-01</i>	COY	Refused	Statute of limitations	
46.	<i>Постановление ФАС Московского округа от 14.08.01 по делу N. КГ-А40/4184-01</i>	COY	Refused	Statute of limitations	

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S.84 JSCA invalidity (last known outcome)	Grounds	Observations
47.	<i>Постановление ФАС Московского округа от 14.08.01 по делу N. КГ-А40/4246-01</i>	COY	Refused	Statute of limitations	Insolvency claim
48.	<i>Постановление ФАС Московского округа от 15.03.01 по делу N. КГ-А40/979-01; Постановление ФАС Московского округа от 27.08.01 по делу N. КГ-А40/4435-01</i>	COY	Refused	Section 83 approval obtained	
49.	<i>Постановление ФАС Московского округа от 29.08.01 по делу N. КГ-А40/4580-01</i>	COY	Refused	Section 81 conflict not established	
50.	<i>Постановление ФАС Московского округа от 12.09.01 по делу N. КГ-А40/4892-01</i>	SHR	Granted	Part XI JSCA breach	
51.	<i>Постановление ФАС Московского округа от 18.09.01 по делу N. КГ-А40/5058-01</i>	SHR	Refused	Section 81 conflict not established; Breach of claimant's rights not established	
52.	<i>Постановление ФАС Московского округа от 18.09.01 по делу N. КГ-А40/5120-01-1</i>	COY	Retrial: Grant reversed	Presence of Part XI JSCA approval insufficiently examined by lower courts	Insolvency claim
53.	<i>Постановление ФАС Московского округа от 02.10.01 по делу N. КГ-А40/5398-01</i>	SHR	Refused	Contemporaneous ownership rule	
54.	<i>Постановление ФАС Московского округа от 10.10.01 по делу N. КГ-А40/5568-01</i>	COY	Refused	Section 83 approval obtained	

Case Dataset No	FAC Decision(s)	Claimants: COY/SHR	S.84 JSCA invalidity (last known outcome)	Grounds	Observations
55.	<i>Постановление ФАС Московского округа от 06.12.01 по делу N. КГ-А41/7068-01</i>	COY	Refused	Section 81 conflict not established	Insolvency claim
56.	<i>Постановление ФАС Московского округа от 21.12.01 по делу N. КГ-А40/7393-01</i>	COY	Refused	Statute of limitations	
57.	<i>Постановление ФАС Московского округа от 19.09.01 по делу N. КГ-А40/5121-01; Постановление ФАС Московского округа от 16.01.02 по делу N. КГ-А40/8016-01</i>	SHR	Refused	Section 81 transaction not established; Breach of claimant's rights not established	
58.	<i>Постановление ФАС Московского округа от 23.01.02 по делу N. КГ-А40/8298-01</i>	COY	Granted	Non- Part XI JSCA grounds (Part XI unavailable due to statute of limitations)	Insolvency claim
59.	<i>Постановление ФАС Московского округа от 06.02.02 по делу N. КГ-А40/117-02</i>	COY	Granted	Part XI JSCA breach	Insolvency claim
60.	<i>Постановление ФАС Московского округа от 14.02.02 по делу N. КГ-А41/487-02</i>	SHR	Refused	Section 81 transaction not established	
61.	<i>Постановление ФАС Московского округа от 14.02.02 по делу N. КГ-А41/487-02</i>	COY	Granted	Part XI JSCA breach	
62.	<i>Постановление ФАС Московского округа от 06.09.01 по делу N. КГ-А41/4849-01; Постановление ФАС Московского округа от 26.03.02 по делу N. КГ-А41/1625-02</i>	COY	Refused	Section 83 approval obtained	Insolvency claim

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S.84 JSCA invalidity (last known outcome)	Grounds	Observations
63.	<i>Постановление ФАС Московского округа от 11.04.02 по делу N. КГ-А40/1879-02 ; Постановление ФАС Московского округа от 11.04.02 по делу N. КГ-А40/1946-02</i>	SHR	Refused	Section 81 transaction not established; Breach of claimant's rights not established	
64.	<i>Постановление ФАС Московского округа от 16.04.02 по делу N. КГ-А40/2189-02</i>	COY	Granted	Part XI JSCA breach	
65.	<i>Постановление ФАС Московского округа от 18.04.02 по делу N. КГ-А40/1829-02</i>	COY	Refused	Section 81 transaction not established	
66.	<i>Постановление ФАС Московского округа от 16.05.02 по делу N. КГ-А40/3007-02</i>	SHR	Granted	Part XI JSCA breach	
67.	<i>Постановление ФАС Московского округа от 30.05.02 по делу N. КГ-А40/3309-02</i>	SHR	Refused	Statute of limitations; Breach of claimant's rights not established	
68.	<i>Постановление ФАС Московского округа от 18.07.02 по делу N. КГ-А40/4546-02</i>	COY	Refused	Statute of limitations	Insolvency claim
69.	<i>Постановление ФАС Московского округа от 7.08.02 по делу N. КГ-А40/4993-02</i>	SHR	Refused	Section 83 approval obtained	
70.	<i>Постановление ФАС Московского округа от 7.08.02 по делу N. КГ-А40/5080-02</i>	COY	Refused	Statute of limitations	

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S 84 JSCA invalidity (last known outcome)	Grounds	Observations
71.	<i>Постановление ФАС Московского округа от 13.08.02 по делу N. КГ-А40/5213-02</i>	COY	Refused	Statute of limitations	
72.	<i>Постановление ФАС Московского округа от 16.09.02 по делу N. КГ-А41/6025-02</i>	COY	Refused	Section 81 transaction not established	
73.	<i>Постановление ФАС Московского округа от 26.09.02 по делу N. КГ-А40/5499-02</i>	SHR	Refused	Section 81 transaction not established	
74.	<i>Постановление ФАС Московского округа от 02.10.02 по делу N. КГ-А41/6504-02</i>	COY	Refused	Statute of limitations	Insolvency claim
75.	<i>Постановление ФАС Московского округа от 09.10.02 по делу N. КГ-А40/6913-02</i>	COY	Granted	Part XI JSCA breach	
76.	<i>Постановление ФАС Московского округа от 18.12.02 по делу N. КГ-А40/8251-02</i>	SHR	Refused	Section 83 approval obtained	
77.	<i>Постановление ФАС Московского округа от 09.01.03 по делу N. КГ-А41/8616-02</i>	SHR	Retrial: Refusal reversed	Lower courts erred in denying shareholder standing in section 84 suit	D1 supports claim
78.	<i>Постановление ФАС Московского округа от 15.01.03 по делу N. КГ-А41/8615-02</i>	SHR	Retrial: Refusal reversed	Lower courts erred in denying shareholder standing in section 84 suit	D1 supports claim

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S.84 JSCA invalidity (last known outcome)	Grounds	Observations
79.	<i>Постановление ФАС Московского округа от 04.02.03 по делу N. КГ-А40/69-03</i>	SHR	Refused	Contemporaneous ownership rule; Breach of claimant's rights not established	
80.	<i>Постановление ФАС Московского округа от 25.02.03 по делу N. КГ-А41/8816-02</i>	SHR	Retrial: Grant reversed	No evidence of shareholding examined by lower courts; Contracts rescinded without pleadings; Breach of claimant's rights not established	D1 supports claim
81.	<i>Постановление ФАС Московского округа от 21.03.03 по делу N. КГ-А40/382-03</i>	SHR	Refused	Statute of limitations	D1 supports claim
82.	<i>Постановление ФАС Московского округа от 02.04.03 по делу N. КГ-А40/1719-03</i>	SHR	Refused	Section 81 transaction not established	
83.	<i>Постановление ФАС Московского округа от 23.04.03 по делу N. КГ-А40/718-03</i>	COY	Refused	Statute of limitations	Insolvency claim
84.	<i>Постановление ФАС Московского округа от 22.05.03 по делу N. КГ-А40/3275-03</i>	COY	Refused	Section 81 conflict not established	
85.	<i>Постановление ФАС Московского округа от 26.09.00 по делу N. КГ-А40/4349-00; Постановление ФАС Московского округа от 17.06.03 по делу N. КГ-А40/3840-03-П</i>	COY	Refused	Statute of limitations	Insolvency claim
86.	<i>Постановление ФАС Московского округа от 17.06.03 по делу N. КГ-А40/3766-03</i>	COY	Refused	Statute of limitations	Insolvency claim

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S 84 JSCA invalidity (last known outcome)	Grounds	Observations
87.	<i>Постановление ФАС Московского округа от 30.06.03 по делу N. КГ-А40/4022-03</i>	SHR	Refused	Contemporaneous ownership rule; Breach of claimant's rights not established	D1 supports claim
88.	<i>Постановление ФАС Московского округа от 09.07.03 по делу N. КГ-А40/4498-03</i>	SHR	Refused	Statute of limitations	
89.	<i>Постановление ФАС Московского округа от 14.07.03 по делу N. КГ-А41/4709-03</i>	SHR	Retrial: Refusal reversed	Lower courts insufficiently investigated claimant's knowledge under statute of limitations	D1 supports claim
90.	<i>Постановление ФАС Московского округа от 15.07.03 по делу N. КГ-А40/4617-03</i>	SHR	Refused	Section 81 transaction not established; Breach of claimant's rights not established	
91.	<i>Постановление ФАС Московского округа от 14.08.03 по делу N. КГ-А41/5432-03</i>	SHR	Refused	Section 81 conflict not established	
92.	<i>Постановление ФАС Московского округа от 28.08.03 по делу N. КГ-А40/6214-03</i>	COY	Refused	Statute of limitations	Insolvency claim
93.	<i>Постановление ФАС Московского округа от 03.09.03 по делу N. КГ-А40/6249-03</i>	SHR	Refused	Breach of claimant's rights not established	
94.	<i>Постановление ФАС Московского округа от 14.02.03 по делу N. КГ-А40/45-03; Постановление ФАС Московского округа от 03.09.03 по делу N. КГ-А41/6360-03</i>	SHR	Granted	Part XI JSCA breach	D1 supports claim

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S.84 JSCA invalidity (last known outcome)	Grounds	Observations
95.	<i>Постановление ФАС Московского округа от 17.09.03 по делу N. КГ-А40/6877-03</i>	SHR	Retrial: Refusal reversed	Lower courts insufficiently investigated circumstances pertinent to statute of limitations	
96.	<i>Постановление ФАС Московского округа от 08.10.03 по делу N. КГ-А40/7761-03</i>	SHR	Refused	Section 81 conflict not established; Breach of claimant's rights not established	
97.	<i>Постановление ФАС Московского округа от 10.10.03 по делу N. КГ-А40/7702-03</i>	SHR	Refused	Section 81 conflict not established; Breach of claimant's rights not established	
98.	<i>Постановление ФАС Московского округа от 21.10.03 по делу N. КГ-А40/8200-03</i>	COY	Refused	Statute of limitations	Insolvency claim
99.	<i>Постановление ФАС Московского округа от 21.10.03 по делу N. КГ-А40/8244-03</i>	COY	Refused	Statute of limitations	Insolvency claim
100.	<i>Постановление ФАС Московского округа от 31.10.03 по делу N. КГ-А40/8334-03-1,2</i>	SHR	Granted	Part XI JSCA breach	D1 supports claim
101.	<i>Постановление ФАС Московского округа от 11.11.03 по делу N. КГ-А40/8835-03;</i>	COY	Refused	Section 81 conflict not established	
102.	<i>Постановление ФАС Московского округа от 19.11.03 по делу N. КГ-А40/9169-03</i>	SHR	Refused	Breach of claimant's rights not established	D1 supports claim

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S 84 JSCA invalidity (last known outcome)	Grounds	Observations
103.	<i>Постановление ФАС Московского округа от 28.11.03 по делу N. КГ-А40/9371-03</i>	SHR	Refused	Section 81 conflict not established	D1 supports claim
104.	<i>Постановление ФАС Московского округа от 10.05.01 по делу N. КГ-А40/2167-01; Постановление ФАС Московского округа от 19.02.03 по делу N. КГ-А40/200-03-П; Постановление ФАС Московского округа от 4.12.03 по делу N. КГ-А40/9674-03-П</i>	COY	Granted	Part XI JSCA breach	Insolvency claim
105.	<i>Постановление ФАС Московского округа от 05.12.03 по делу N. КГ-А41/9659-03</i>	SHR	Refused	Section 81 conflict not established	
106.	<i>Постановление ФАС Московского округа от 08.12.03 по делу N. КГ-А40/9604-03</i>	SHR	Refused	Statute of limitations	
107.	<i>Постановление ФАС Московского округа от 8.12.03 по делу N. КГ-А40/9796-03</i>	COY	Granted	Part XI JSCA breach	
108.	<i>Постановление ФАС Московского округа от 24.12.03 по делу N. КГ-А40/10273-03</i>	COY	Granted	Part XI JSCA breach	
109.	<i>Постановление ФАС Московского округа от 30.12.03 по делу N. КГ-А41/10363-03</i>	SHR	Retrial: Refusal reversed	Lower courts insufficiently investigated claimant's knowledge under statute of limitations	D1 supports claim

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S 84 JSCA invalidity (last known outcome)	Grounds	Observations
110.	<i>Постановление ФАС Московского округа от 06.01.04 по делу N. КГ-А40/10509-03</i>	SHR	Refused	Section 81 transaction not established	D1 supports claim
111.	<i>Постановление ФАС Московского округа от 24.02.04 по делу N. КГ-А40/599-04</i>	SHR	Retrial: Grant reversed	Incorrect accounts used to value transaction	
112.	<i>Постановление ФАС Московского округа от 25.02.04 по делу N. КГ-А40/811-04</i>	SHR	Retrial: Grant reversed	Incorrect accounts used to value transaction	
113.	<i>Постановление ФАС Московского округа от 16.03.04 по делу N. КГ-А40/476-04</i>	SHR	Refused	Section 83 approval obtained	
114.	<i>Постановление ФАС Московского округа от 16.03.04 по делу N. КГ-А40/1371-04</i>	SHR	Refused	Section 81 conflict not established	
115.	<i>Постановление ФАС Московского округа от 16.03.04 по делу N. КГ-А40/1429-04-1,2</i>	SHR	Retrial: Grant reversed	Incorrect accounts used to value transaction; Breach of claimant's rights not established	
116.	<i>Постановление ФАС Московского округа от 29.03.04 по делу N. КГ-А40/2053-04</i>	SHR	Granted	Part XI JSCA breach	
117.	<i>Постановление ФАС Московского округа от 07.04.04 по делу N. КГ-А40/1043-04</i>	SHR	Refused	Section 81 conflict not established; Breach of claimant's rights not established	

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S 84 JSCA invalidity (last known outcome)	Grounds	Observations
118.	<i>Постановление ФАС Московского округа от 14.04.04 по делу N. КГ-А40/2088-04</i>	SHR	Retrial: Grant reversed	Lower instances did not establish whether claimant held shares contemporaneously with transaction	
119.	<i>Постановление ФАС Московского округа от 22.04.04 по делу N. КГ-А40/2630-04</i>	SHR	Refused	Section 81 transaction not established; Breach of claimant's rights not established	
120.	<i>Постановление ФАС Московского округа от 26.04.04 по делу N. КГ-А41/2963-04</i>	SHR	Retrial: Grant reversed	Contemporaneous ownership rule; Breach of claimant's rights not established	
121.	<i>Постановление ФАС Московского округа от 28.04.04 по делу N. КГ-А40/3222-04</i>	SHR	Refused	Section 81 transaction not established	
122.	<i>Постановление ФАС Московского округа от 30.04.04 по делу N. КГ-А40/3026-04-2</i>	COY	Refused	Statute of limitations	Insolvency claim
123.	<i>Постановление ФАС Московского округа от 30.04.04 по делу N. КГ-А40/3196-04</i>	SHR	Refused	Section 81 conflict not established	
124.	<i>Постановление ФАС Московского округа от 01.06.04 по делу N. КГ-А40/4080-04</i>	SHR	Granted	Part XI JSCA breach	

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S.84 JSCA invalidity (last known outcome)	Grounds	Observations
125.	<i>Постановление ФАС Московского округа от 24.04.03 по делу N. КГ-А40/2198-03-Б; Постановление ФАС Московского округа от 18.06.04 по делу N. КГ-А40/2169-04-П</i>	COY	Granted	Part XI JSCA breach	
126.	<i>Постановление ФАС Московского округа от 06.07.04 по делу N. КГ-А40/5317-04</i>	SHR	Refused	Section 81 conflict not established	D1 supports claim
127.	<i>Постановление ФАС Московского округа от 27.07.04 по делу N. КГ-А40/6253-04</i>	SHR	Refused	Statute of limitations	D1 supports claim
128.	<i>Постановление ФАС Московского округа от 26.08.04 по делу N. КГ-А40/7182-04</i>	SHR	Granted	Part XI JSCA breach	
129.	<i>Постановление ФАС Московского округа от 29.09.04 по делу N. КГ-А40/8406-04</i>	SHR	Refused	Section 83 approval obtained	
130.	<i>Постановление ФАС Московского округа от 5.10.04 по делу N. КГ-А40/8874-04</i>	COY	Refused	Statute of limitations	
131.	<i>Постановление ФАС Московского округа от 14.10.04 по делу N. КГ-А40/9131-04</i>	SHR	Refused	Contemporaneous ownership rule	D1 supports claim
132.	<i>Постановление ФАС Московского округа от 27.10.04 по делу N. КГ-А40/9612-04</i>	COY	Refused	Section 81 conflict not established	

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S 84 JSCA invalidity (last known outcome)	Grounds	Observations
133.	<i>Постановление ФАС Московского округа от 09.11.04 по делу N. КГ-А41/9859-04</i>	SHR	Retrial: Refusal reversed	Presence of Part XI JSCA conflict insufficiently examined by lower courts	
134.	<i>Постановление ФАС Московского округа от 24.12.04 по делу N. КГ-А40/11825-04</i>	SHR	Refused	Section 81 conflict not established; Breach of claimant's rights not established	
135.	<i>Постановление ФАС Московского округа от 28.12.04 по делу N. КГ-А40/12155-04</i>	SHR	Retrial: Grant reversed	Presence of Part XI JSCA conflict insufficiently examined by lower courts	
136.	<i>Постановление ФАС Московского округа от 24.01.05 по делу N. КГ-А41/12661-04</i>	COY	Refused	Statute of limitations	
137.	<i>Постановление ФАС Московского округа от 17.03.05 по делу N. КГ-А40/1366-05</i>	SHR	Refused	Breach of claimant's rights not established	
138.	<i>Постановление ФАС Московского округа от 24.03.05 по делу N. КГ-А40/1615-05</i>	SHR	Retrial: Refusal reversed	Lower courts erred in denying remedy when a resolution rather than contract was challenged	
139.	<i>Постановление ФАС Московского округа от 02.06.05 по делу N. КГ-А40/4035-05</i>	SHR	Retrial: Grant reversed	Presence of Part XI JSCA conflict insufficiently examined by lower courts	

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S.84 JSCA invalidity (last known outcome)	Grounds	Observations
140.	<i>Постановление ФАС Московского округа от 6.06.05 по делу N. КГ-А40/4439-05</i>	COY	Granted	Part XI JSCA breach	
141.	<i>Постановление ФАС Московского округа от 07.06.05 по делу N. КГ-А40/4554-05</i>	SHR	Refused	Statute of limitations; Breach of claimant's rights not established	
142.	<i>Постановление ФАС Московского округа от 24.06.05 по делу N. КГ-А40/4653-05</i>	SHR	Refused	Statute of limitations; Breach of claimant's rights not established	
143.	<i>Постановление ФАС Московского округа от 31.08.05 по делу N. КГ-А40/7967-05</i>	SHR	Refused	Breach of claimant's rights not established	D1 supports claim
144.	<i>Постановление ФАС Московского округа от 12.09.05 по делу N. КГ-А40/8576-05</i>	SHR	Refused	Section 81 conflict not established; Breach of claimant's rights not established	
145.	<i>Постановление ФАС Московского округа от 28.02.05 по делу N. КГ-А40/900-04; Постановление ФАС Московского округа от 5.10.05 по делу N. КГ-А41/9300-05</i>	COY	Refused	Section 83 approval obtained	Insolvency claim
146.	<i>Постановление ФАС Московского округа от 14.10.05 по делу N. КГ-А41/9117-05</i>	SHR	Refused	Section 83 approval obtained; Breach of claimant's rights not established	

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S. 84 JSCA invalidity (last known outcome)	Grounds	Observations
147.	<i>Постановление ФАС Московского округа от 27.12.04 по делу N. КГ-А40/11700-04; Постановление ФАС Московского округа от 2.11.05 по делу N. КГ-А40/10317-05-ПБ</i>	COY	Refused	Statute of limitations	Insolvency claim
148.	<i>Постановление ФАС Московского округа от 17.11.05 по делу N. КГ-А40/11191-05</i>	SHR	Granted	Part XI JSCA breach	D1 supports claim
149.	<i>Постановление ФАС Московского округа от 22.11.05 по делу N. КГ-А40/11320-05</i>	SHR	Refused	Section 81 conflict not established	
150.	<i>Постановление ФАС Московского округа от 24.11.05 по делу N. КГ-А41/10274-05</i>	SHR	Refused	Section 83 approval obtained; Breach of claimant's rights not established	
151.	<i>Постановление ФАС Московского округа от 01.12.05 по делу N. КГ-А40/11703-05</i>	SHR	Refused	Statute of limitations; Breach of claimant's rights not established	
152.	<i>Постановление ФАС Московского округа от 14.12.05 по делу N. КГ-А40/11413-05</i>	SHR	Refused	Section 81 conflict not established	
153.	<i>Постановление ФАС Московского округа от 20.12.05 по делу N. КГ-А41/12386-05</i>	SHR	Refused	Section 83 approval obtained; Breach of claimant's rights not established	
154.	<i>Постановление ФАС Московского округа от 20.01.06 по делу N. КГ-А40/13482-05</i>	SHR	Refused	Statute of limitations; Breach of claimant's rights not established	D1 supports claim

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S.84 JSCA invalidity (last known outcome)	Grounds	Observations
155.	<i>Постановление ФАС Московского округа от 26.01.06 по делу N. КГ-А40/13759-05</i>	SHR	Refused	Statute of limitations; Breach of claimant's rights not established	D1 supports claim
156.	<i>Постановление ФАС Московского округа от 15.05.06 по делу N. КГ-А40/3360-06</i>	COY	Granted	Part XI JSCA breach	Insolvency claim
157.	<i>Постановление ФАС Московского округа от 25.05.06 по делу N. КГ-А40/4607-06</i>	COY	Refused	Statute of limitations	
158.	<i>Постановление ФАС Московского округа от 20.06.06 по делу N. КГ-А41/5280-06</i>	COY	Refused	Section 81 conflict not established	
159.	<i>Постановление ФАС Московского округа от 20.06.06 по делу N. КГ-А40/5526-06</i>	COY	Refused	Statute of limitations	
160.	<i>Постановление ФАС Московского округа от 12.07.06 по делу N. КГ-А40/6138-06</i>	SHR	Refused	Section 81 conflict not established	
161.	<i>Постановление ФАС Московского округа от 18.07.06 по делу N. КГ-А40/6004-06</i>	COY	Granted	Part XI JSCA breach	
162.	<i>Постановление ФАС Московского округа от 19.07.06 по делу N. КГ-А40/4949-06</i>	SHR	Retrial: Refusal reversed	Presence of Part XI JSCA approval insufficiently examined by lower courts	
163.	<i>Постановление ФАС Московского округа от 24.07.06 по делу N. КГ-А40/6665-06</i>	SHR	Refused	Section 81 transaction not established	

Case Dataset No.	FAC Decision(s)	Claimants: COY/SHR	S.84 JSCA invalidity (last known outcome)	Grounds	Observations
164.	<i>Постановление ФАС Московского округа от 06.09.06 по делу N. КГ-А40/7961-06</i>	SHR	Retrial: Grant reversed	Breach of claimant's rights not established	
165.	<i>Постановление ФАС Московского округа от 3.10.06 по делу N. КГ-А40/9441-06</i>	COY	Granted	Part XI JSCA breach	
166.	<i>Постановление ФАС Московского округа от 26.04.06 по делу N. КГ-А41/3073-06; Постановление ФАС Московского округа от 05.10.06 по делу N. КГ-А41/9607-06-II</i>	SHR	Refused	Section 81 conflict not established; Breach of claimant's rights not established	
167.	<i>Постановление ФАС Московского округа от 30.10.06 по делу N. КГ-А40/10485-06</i>	SHR	Refused	Section 81 conflict not established; Breach of claimant's rights not established	
168.	<i>Постановление ФАС Московского округа от 8.11.06 по делу N. КГ-А40/10690-06</i>	SHR	Refused	Section 83 approval obtained	
169.	<i>Постановление ФАС Московского округа от 19.12.06 по делу N. КГ-А41/12370-06</i>	SHR	Refused	Section 81 conflict not established; Breach of claimant's rights not established	
170.	<i>Постановление ФАС Московского округа от 28.12.06 по делу N. КГ-А40/12266-06</i>	SHR	Refused	Section 83 approval obtained	

APPENDIX 3

OTHER JUDICIAL DECISIONS CITED IN THE THESIS

EUROPEAN COURT OF HUMAN RIGHTS

Denisov v. Russia (no. 33408/03, 6 May 2004)

Berdzenishvili v. Russia (no. 31697/03, 29 January 2004)

CONSTITUTIONAL COURT OF THE RUSSIAN FEDERATION

Постановление Конституционного Суда Российской Федерации от 10.04.2003 по делу о проверке конституционности пункта 1 статьи 84 Федерального закона Об акционерных обществах в связи с жалобой открытого акционерного общества Приаргунское.

SUPREME ARBITRAZH COURT OF THE RUSSIAN FEDERATION

Постановление Президиума ВАС РФ от 18.01.00 No.6309/99

Постановление Президиума ВАС РФ от 19.09.00 No.1873/00

Постановление Президиума ВАС РФ от 31.10.00 No.3020/00

Постановление Президиума ВАС РФ от 26.04.02 No.7030/01

Постановление Президиума ВАС РФ от 12.11.02 No.6288/02

Постановление Президиума ВАС РФ от 21.10.03 No.10030/03

Постановление Президиума ВАС РФ от 02.12.03 No.9736/03

Постановление Президиума ВАС РФ от 09.12.03 No.12258/03

Постановление Президиума ВАС РФ от 03.02.04 No.13732/03

Постановление Президиума ВАС РФ от 14.10.05 No.12407/06

Постановление Президиума ВАС РФ от 29.03.06 No.2868/06

Постановление Президиума ВАС РФ от 19.04.06 No.3600/06

Постановление Президиума ВАС РФ от 05.12.06 No.9675/06

FEDERAL ARBITRAZH COURTS OF THE RUSSIAN FEDERATION

Постановление ФАС Московского округа от 9.03.00 по делу N. КГ-А41/782-00

Постановление ФАС Московского округа от 3.04.00 по делу N. КГ-А40/3864-99
Постановление ФАС Московского округа от 6.06.01 по делу N. КГ-А40/2664-01
Постановление ФАС Московского округа от 7.06.01 по делу N. КГ-А40/2787-01
Постановление ФАС Московского округа от 20.06.01 по делу N. КГ-А40/2961-01
Постановление ФАС Московского округа от 21.06.01 по делу N. КГ-А40/2963-01
Постановление ФАС Московского округа от 23.10.01 по делу N. КГ-А40/5957-01
Постановление ФАС Московского округа от 6.12.01 по делу N. КГ-А40/7132-01
Постановление ФАС Московского округа от 31.01.02 по делу N. КГ-А40/4-02
Постановление ФАС Московского округа от 4.03.02 по делу N. КГ-А40/918-02
Постановление ФАС Московского округа от 29.04.02 по делу N. КГ-А40/2426-02
Постановление ФАС Московского округа от 11.07.02 по делу N. КГ-А40/4393-02
Постановление ФАС Московского округа от 11.07.02 по делу N. КГ-А40/4394-02
Постановление ФАС Московского округа от 11.07.02 по делу N. КГ-А40/4395-02
Постановление ФАС Московского округа от 17.03.03 по делу N. КГ-А40/1282-03
Постановление ФАС Московского округа от 31.03.03 по делу N. КГ-А40/374-03
Постановление ФАС Московского округа от 20.06.03 по делу N. КГ-А40/3784-03
Постановление ФАС Московского округа от 7.10.03 по делу N. КГ-А40/7570-03
Постановление ФАС Северо-Кавказского округа от 22.12.03 по делу N. Ф08-4352/2003
Постановление ФАС Московского округа от 21.10.04 по делу N. КГ-А40/9027-04
Постановление ФАС Московского округа от 25.05.06 по делу N. КГ-А40/4607-06

COMMON LAW COURTS

Foss v. Harbottle (1843) 67 ER 189
Burland v. Earle [1902] AC 83
Boardman v. Phipps [1967] 2 AC 46
Jordan v. Duff & Phelps 815 F.2d 429 (7th Circuit, 1987)
Eurocruit Europe Ltd, RE [2007] 2 BCLC 598

BIBLIOGRAPHY

Administration of the Russian Federation, *Concept for the Development of Corporate Legislation for the period to 2008* [Администрация РФ, Концепция развития корпоративного законодательства на период до 2008 года], (2005)

Akerlof G, 'The Market for Lemons: Qualitative Uncertainty and the Market Mechanism' (1970) 84 *Quarterly Journal of Economics* 488

Alexandridis, G., Petmezas, D., and Travlos, N. G., 'Gains from Mergers and Acquisitions around the World: New Evidence' (2010) *Financial Management* 1671

Anderlini, L., and Felli, L., 'Incomplete Written Contracts: Undescribable States of Nature' (1994) 66 *Review of Economic Studies* 83.

Andreev, V., 'The Privatization of State Enterprises in Russia' (1992) 18 *Review of Central and East European Law* 265

Angblad, J. et al, 'Ownership and Control In Sweden: Strong Owners, Weak Minorities and Social Control in Barca, F., and Becht, M., (eds), *The Control of Corporate Europe*, (Oxford University Press, 2001) p.p. 228 – 257

Aoki, M., and Kim, H-K., 'Controlling Insider Control: Issues of Corporate Governance in Transitional Economies', in *Corporate Governance in Transitional Economies: Insider Control and the Role of Banks*, (EDI Developmental Studies, the World Bank, 1995)

Armour, J., and Whincop, J., 'The Proprietary Foundations of Corporate Law' (2007) 27 *Oxford Journal of Legal Studies* 429

Armour, J., Black, B., Cheffins, B., and Nolan, R., 'Private Enforcement of Corporate Law: An Empirical Comparison of the United Kingdom and the United States' (2009) 6 *Journal of Empirical Legal Studies* 687

Atiyah, P., *The Rise and Fall of Freedom of Contract*, (Oxford University Press, 1979)

Ayres, I., 'Making a Difference: The Contractual Contributions of Easterbrook and Fischel' (1992) 59 *The University of Chicago Law Review* 1391

Ayres, I., 'Protecting Property with Puts' (1998) 32 *Valparaiso University Law Review* 793

Ayres, I., *Optional Law: The Structure of Legal Entitlements*, (The University of Chicago Press, 2005)

Ayres, I., and Gertner, R., 'Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules' (1989) 99 *The Yale Law Journal* 87

Ayres, I., and Gertner, R., 'Strategic Contractual Inefficiency and the Optimal Choice of Legal Rules' (1991) 101 *The Yale Law Journal* 729

- Ayres, I., and Talley, E., 'Solomonic Bargaining: Dividing a Legal Entitlement to Facilitate Coasean Trade' (1994) 104 *The Yale Law Journal* 1027
- Ayres, I., and Talley, E., 'Distinguishing Between Consensual and Nonconsensual Advantages of Liability Rules' (1995) 105 *The Yale Law Journal* 235
- Ayres, I., and Balkin, J., 'Legal Entitlements as Auctions: Property Rules, Liability Rules, and Beyond' (1996) 106 *The Yale Law Journal* 703
- Baird and Jackson, 'Fraudulent Conveyance Law and its Proper Domain' (1985) 38 *Vanderbilt Law Review* 829
- Baldwin, R., *Rules and Government*, (Oxford University Press, 1995)
- Baldwin, R., and Cave. M., *Understanding Regulation: Theory, Strategy and Practice*, (Oxford University Press, 1999)
- Barca, F., and Becht, M., (eds), *The Control of Corporate Europe*, (Oxford University Press, 2001)
- Bauer, M. W., and Gaskell, G., *Qualitative Researching with Text, Image and Sound: A Practical Handbook*, (Sage Publications, 2000)
- Beatson, J., and Friedmann, D., *Good Faith and Fault in Contract Law*, (Oxford University Press, 1995)
- Bebchuk, L., 'Efficient and Inefficient Sales of Corporate Control' (1994) 109(4) *The Quarterly Journal of Economics* 957
- Bebchuk, L., and Shavell, S., 'Information and the Scope of Liability for Breach of Contract' (1991) 7(2) *Journal of Law, Economics, and Organization* 284
- Bebchuk, L., and Shavell, S., 'Reconsidering Contractual Liability and the Incentive to Reveal Information' (1998) 51 *Stanford Law Review* 1615
- Bebchuck, L., 'A rent-protection theory of corporate control and ownership' (1999) NBER Working Paper
- Bebchuk, L., and Hamdani, A., 'The Elusive Quest for Global Governance Standards' (2009) 157 *University of Pennsylvania Law Review* 1263
- Becht, M., and Roell, A., 'Blockholdings in Europe: An International Comparison' (1999) 43 *European Economic Review* 1049
- Belov, V., et al, *Corporate Law: Current Problems of Theory and Practice*, [Белов В., *Корпоративное право: актуальные проблемы теории и практики*] (URAIT, 2009)

- Ben-Sharar, O., 'Agreeing to Disagree: Filling Gaps in Deliberately Incomplete Contracts' (2004) 36 American Law & Economics Association Annual Meetings 1
- Berglof, E., 'What Do Firms Disclose and Why? Enforcing Corporate Governance and Transparency in Central and Eastern Europe' (2005) 21 Oxford Review of Economic Policy 178
- Bernstein, L., 'Merchant Law in a Merchant Court: Rethinking the Code's Search for Immanent Business Norms' (1996) 144 University of Pennsylvania Law Review 1765
- Beveridge, N., 'The Corporate Director's Fiduciary Duty of Loyalty: Understanding the Self-Interested Director Transaction' (1992) 41 Depaul Law Review 655
- Black B., 'Is corporate law trivial?: A political and economic analysis' (1990) 84 NorthWestern University Law Review 542
- Black, B., 'Legal and Institutional Preconditions for Strong Securities Markets' (2001) 48 UCLA Law Review 781
- Black, B., and Kraakman, R., 'A Self-Enforcing Model of Corporate Law' (1995) 109 Harvard Law Review 1911
- Black, B., Kraakman, R., and Tarassova, A., *Guide to the Russian Law on Joint Stock Companies*, (Kluwer Law International, 1998)
- Black, B., Kraakman, R., and Tarassova, A., 'Russian Privatization and Corporate Governance: What Went Wrong?' (2000) 52 Stanford Law Review 1731
- Black, B., Love, I., and Rachinsky, A., 'Corporate Governance Indices and Firms' Market Values: Times Series Evidence from Russia' (2006a) 7 Emerging Markets Review 361
- Black, B., et al, *Comparative Analysis on Legal Regulation of the Liability of Members of the Management Organs of Companies*, (Report to Russian Center for Capital Market Development, 2006b)
- Bogart, W., *Consequences: The Impact of Law and Its Complexity*, (University of Toronto Press, 2002)
- Boyle, A., *Minority Shareholders' Remedies* (Cambridge University Press, 2002)
- Braginskii, M. S., 'Legal Regulation of Entrepreneurship in the Russian Federation' (1993) 19 Review of Central and East European Law 365
- Bratton, W., 'The New Economic Theory of the Firm: Critical Perspectives from History' (1988) 41 Stanford Law Review 1471

- Bratton, W., 'Game Theory and the Restoration of Honor to Corporate Law's Duty of Loyalty', in Mitchell, L. E., *Progressive Corporate Law* (Westview Press, 1995)
- Bratton, W., and McCahery, J., 'Comparative Corporate Governance and the Theory of the Firm: The Case Against Global Cross Reference' (1999) 38 *Columbia Journal of Transnational Law* 213
- Bratton, W., and McCahery, J., 'Incomplete Contracts Theories of the Firm and Comparative Corporate Governance' (2001) 2 *Theoretical Enquiries in Law* 745
- Bromwich, M., *Financial Reporting, Information and Capital Markets*, (Pearson Education, 1992)
- Brudney, V., 'Contract and Fiduciary Duty in Corporate Law' (1997) 38 *Boston College Law Review* 595
- Budylin, S., 'Transaction of Commercial Societies, in the Completion of which there is a Conflict of Interest' [Будылин, С., Сделки хозяйственных обществ, в совершении которых имеется заинтересованность] (2005) 7 *Arbitrazh Practice* 14
- Calabresi, G., and Melamed, A., 'Property Rules, Liability Rules, and Inalienability: One View of the Cathedral' (1972) 85 *Harvard Law Review* 1089
- Chaika, F., 2005, Gazprom – Rosneft: no conflict, no merger [Чайка, Ф., Газпром - Роснефть: ни конфликта, ни слияния], *Izvestia*, 16 February, available at <http://www.izvestia.ru/news/299774>. Accessed on 6 March 2014
- Chander, A., 'Minorities, Shareholder and Otherwise' (2003) 113 *The Yale Law Journal* 119
- Cheffins, B., *Company Law: Theory, Structure and Operation*, (Oxford University Press, 1997)
- Cheffins, B., 'Does law matter? The separation of ownership and control in the United Kingdom' (2001) 30 *Journal of Legal Studies* 459
- Cheffins B., 'Putting Britain on the Roe Map: the Emergence of the Berle-Means Corporation in the United Kingdom in McCahery et al (eds.), *Corporate Governance Regimes*, (Oxford University Press, 2002) p.p. 147 – 172
- Chernykh, L., 'Ultimate Ownership and Control in Russia' (2008) 88 *Journal of Financial Economics* 169
- Clark, R. C., *Corporate Law*, (Little, Brown & Company, 1986)
- Clemen, R., and Reilly, T., *Making Hard Decisions*, (Duxbury, Thomson Learning, 2001)
- Coase, R., *The Firm, the Market, and the Law*, (University of Chicago Press, 1988).

Coffee, J. C. Jr., 'The Survival of the Derivative Suit: An Evaluation and a Proposal for Legislative Reform' (1981) 81 Columbia Law Review 261

Coffee, J. C. Jr., 'Regulating the Market for Corporate Control' (1984) 84 Columbia Law Review 1145

Coffee, J. C. Jr., 'The Unfaithful Champion: The Plaintiff as Monitor in Shareholder Litigation' (1985) 48 Law & Contemporary Problems 5

Coffee, J. C. Jr., 'Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law through Class and Derivative Actions' (1986) 86 Columbia Law Review 669

Coffee, J. C. Jr., 'The Mandatory/ Enabling Balance in Corporate Law: An Essay on The Judicial Role' (1989) 89 Columbia Law Review 1618

Coffee, J. C. Jr., 'Liquidity Versus Control: The Institutional Investor as Corporate Monitor' (1991) 91 Columbia Law Review 1278

Coffee, J. C. Jr., *The Rise of Dispersed Ownership* (2001) 111 Yale Law Journal 1

Coffee, J. C. Jr., *Convergence and its Critics: What are the Preconditions to the Separation of Ownership and Control?* in McCahery J., et al (eds.), *Corporate Governance Regimes*, (Oxford University Press, 2002) p.p. 93-100

Cohen, D., and Knetsch, J., 'Judicial Choice and Disparities between Measures of Economic Values' (1992) 30 Osgoode Hall Law Journal 737

Cohen, G., 'The Negligence-Opportunism Trade off in Contract Law' (1991) 20 Hofstra Law Review 941

Collins, H., *Regulating Contracts*, (Oxford University Press, 1999)

Conac, P-H., Enriques, L., Gelter, M., 'Constraining Dominant Shareholders' Self-Dealing: The Legal Framework in France, Germany and Italy' (2008) ECGI Working Paper No. 18

Conaglen, M., 'The Nature and Function of Fiduciary Loyalty' (2005) Law Quarterly Review 1

Cooter, R., 'Unity in Tort, Contract and Property: The Model of Precaution' (1985) 73 California Law Review 1

Cooter, R., and Freedman, B., 'The Fiduciary Relationship: Its Economic Character and Legal Consequences' (1991) 66 New York University Law Review 1045

Cooter, R., and Ulen, T., *Law & Economics*, 4th edn. (Pearson Education, 2004)

Dahan, F., and Dine, J., 'Transplantation for Transition – Discussion on a Concept Around Russian Reform of the Law on Reorganisation' (2003) 23 Legal Studies 284

Dahlman C., The problem of externality (1979) 22 Journal of Law and Economics 148.

Dammann, J., 'Corporate Ostracism: Freezing out Controlling Shareholders' (2007) 33 The Journal of Corporation Law 683

Davis, K., 'Judicial Review of Fiduciary Decision Making – Some Theoretical Perspectives' (1985) 80 Northwestern University Law Review 1

Davis, K. and Kruse, M., 'Taking the Measure of Law: The Case of Doing Business Project' (2007) 32 Law & Social Inquiry 1095

Davies, A., 'The Proprietary Foundations of Corporate Law' (2007) 27 Oxford Journal of Legal Studies 429

Davies, P., *Introduction to Company Law*, (Oxford University Press, 2002)

Davies, P., *Principles of Modern Company Law*, 8th edn. (Sweet & Maxwell, 2008)

Deakin, S., and Hughes, A., 'Economic Efficiency and the Proceduralisation of Company Law' (1999) ESRC Centre for Business Research, University of Cambridge, Working Paper No. 133

Dedov, D., *Conflict of Interests* [Дедов, Д., *Конфликт интересов*], (WoltersKluwer, 2004)

DeMott, D., 'Beyond Metaphor: An Analysis of Fiduciary Obligation' (1988) 1988 Duke Law Journal 879

DeMott, D., 'Book Review: Trust and Tension with Corporations' (1995) 81 Cornell Law Review 1308

Dignam, A., and Galanis, M., *The Globalization of Corporate Governance*, (Ashgate Publishing, 2009)

Diver, C., 'The Optimal Precision of Administrative Rules' (1983) 93 The Yale Law Journal 65

Djankov, S., La Porta, R., Lopez-de-Silanes, F., Shliefer, A., 'The Law and Economics of Self-Dealing' (2008) 88 Journal of Financial Economics 430

Dobrovolskii, V., *Problems of Corporate Law in the Arbitrazh Court Practice* [Добровольский, В., *Проблемы корпоративного права в арбитражной практике*], (Wolters Kluwer, 2006)

Dobrovolskii, V., *Analysis and Commentary on Corporate Legislation and Court Practice* [Добровольский, В., *Анализ и комментарий корпоративного законодательства и судебной практики*], (Wolters Kluwer, 2007)

Dolgopyatova T., *Corporate ownership and control in the Russian companies after the decade of reforms* in Ikemoto S. and Iwasaki I., *Corporate governance in transition economies: the case of Russia*, 2004, Institute of Economic Research Hitotsubashi University, Discussion Paper Series No. 29

Dozortsev, V., 'Trends in the Development of Russian Civil Legislation During the Transition to a Market Economy' (1993) 19 *Review of Central and East European Law* 513

Dyck, A., and Zingales, L., 'Private Benefits of Control: An International Comparison' (2004) 59 *Journal of Finance* 537

Earle, J., 'Post-Privatization Ownership Structure and Productivity in Russian Industrial Enterprises' (1998 version) Stockholm School of Economics 1

Easterbrook, F. and Fischel, D., *The Economic Structure of Corporate Law*, (Harvard University Press, 1991)

Easterbrook, F. and Fischel, R., 'Contract and Fiduciary Duty' (1993) 36 *The Journal of Law and Economics* 425

Edmunds, R. and Lowry, J., 'The Continuing Value of Relief for Directors' Breach of Duty' (2003) 66 *The Modern Law Review* 195

Ellickson, R., *Order Without Law*, (Harvard University Press, 1991)

Enriques, L., 'Off the books, but on the Record: Evidence from Italy on the Relevance of Judges to the Quality of Corporate Law in Italy' in Milhaupt, C., *Global Markets, Domestic Institutions*, (Columbia University Press, 2003)

Enriques, L., 'The Mandatory Bid Rule in the Proposed EC Takeover Directive: Harmonization as Rent-Seeking?' in Ferrarini et al, *Reforming Company and Takeover Law in Europe* (Oxford, 2004)

Ehrlich, I., and Posner, R., 'An Economic Analysis of Legal Rulemaking' (1974) 3 *The Journal of Legal Studies* 257

Eremenko, U., 'Transactions with Conflicts of Interest: the New in Law Application' [Еременко, Ю., *Сделки с заинтересованностью: новеллы правоприменения*] (2007) 10 *Corporate Jurist* 51

Evplanov, A., 2004, Rosneft will be taken over by Gazprom [Евпланов, А., "Роснефть" будет поглощена "Газпромом"], *Rossiyskaya Gazetta*, 21 September, available at <http://www.rg.ru/2004/09/21/sliianie.html>. Accessed on 6 March 2014

Farnsworth, W., *The Legal Analyst*, (University of Chicago Press, 2007)

Faizutdinov, I., 'The Role and Responsibility of the Board of Directors in the Control Over Completion of Substantial Transactions and Transactions Involving Conflicts of Interest in Joint Stock Companies Legislation and Judicio-Arbitrazh Practice' (2001) Report to the Fourth OECD Roundtable on Corporate Governance in Russia

Ferran, E., *Company Law and Corporate Finance*, (Oxford University Press, 1999)

Fischel, D. R. and Bradley, M., 'The Role of Liability Rules and The Derivative Suit in Corporate Law: A Theoretical and Empirical Analysis' (1985) 71 *Cornell Law Review* 261

Flannigan, R., 'The Strict Character of Fiduciary Liability' (2006) *New Zealand Law Review* 209

Fox, D., 'Constructive Notice and Knowing Receipt: An Economic Analysis' (1998) 57 *Cambridge Law Journal* 391

Foucault, M., *The Archaeology of Knowledge and the Discourse on Language*, (Tavistock Publications, 1972)

Fox, M. and Heller, M., 'Corporate Governance Lessons From Russian Enterprise Fiascoes' (2000) 75 *New York University Law Review* 1720

Frants, V., 'Russian Corporate Law: Is 'Self-Enforcement' Still the Way to Go?' (2008) 13 *UCL Journal International Law & Foreign Affairs* 438

Freedland, M., and Davies, P., *Labour Legislation and Public Policy*, (Oxford University Press, 1993)

Frye, T., *Slapping the Grabbing Hand: Credible Commitment and Property Rights in Russia* (2003) GU-VSHE working paper WP1/2003/02

Gabov, A., *Transaction with Conflicts of Interest in Practice of Joint Stock Societies* [Габов, А., *Сделки с заинтересованностью в практике акционерных обществ: проблемы правового регулирования*], (Statut, 2005)

Garth, B. and Sarat. A., *How Does Law Matter? Fundamental Issues in Law and Society Research, Volume 3*, (Northwestern University Press, 1998)

Gilson R. and Kraakman R., *The mechanisms of market efficiency* (1984) 70 *Vanderbilt Law Review* 549

Gilson, R., and Gordon, J., 'Controlling Controlling Shareholders' (2003) 152 University of Pennsylvania Law Review 785

Ginsburg, T., 'Does law matter for economic development?' (2000) 34 Law and Society Review

Glazunov, D., 'The Role of Disclosure in Strengthening Corporate Governance and Accountability' (November 2000, OECD Roundtable)

Godlewski, C., Fungacova, Z., and Weill, L., 'Stock Market Reaction to Debt Financing Arrangements in Russia' (2010) 16 Bofit Discussion Papers 1

Goetz, C. and Scott, R., 'Principles of Relational Contracts' (1981) 67 Virginia Law Review 1089

Gololobov, D., *Joint Stock Society Against a Shareholder: Defence to Corporate Greenmail* [Гололобов, Д., *Акционерное общество против акционера: противодействие корпоративному шантажу*], (YusticInform, 2004)

Goodwin, P. and Wright, G., *Decision Analysis for Management Judgment*, 4th edn. (John Wiley & Sons, 2009)

Goriaev, A., and Zabotkin, A., 'Risks of Investing in the Russian Stock Market: Lessons of the First Decade' (2006) 7 Emerging Markets Review 380

Goshen, Z., 'The Efficiency of Controlling Corporate Self-Dealing: Theory Meets Reality' (2003) 91 California Law Review 393

Gray, C. and Hendley, K., 'Developing Commercial Law in Transition Economies: Examples from Hungary and Russia, in Sachs, J. D., and Pistor, K., *The Rule of Law and Economic Reform in Russia*, (Westview Press, 1997) p.p. 139-164

Grechenig, K. and Sekyra, M., 'No Derivative Shareholder Suits in Europe – A Model of Percentage Limits, Collusion and Residual Owners' (2007) Working Paper No. 312

Griffin, S., 'Problems in the Identification of a Company Director' (2003) 54 Northern Ireland Legal Quarterly 43

Gros, A. and Dedov, D., 'Problems of Implementation of Derivative Claims' [Грось А., Дедов Д., Проблемы реализации косвенных исков], (2007) 3 Zakon 157

Gudieva, A., 'The Notion of Beneficiary and the Grounds for Invalidating Transactions Involving a Conflict of Interest' [Гудиева, А., Понятие выгодоприобретателя и основания признания недействительными сделок с заинтересованностью], (2007) 10 Corporate Jurist 45

- Gunningham, N., and Grabosky, P., *Smart Regulation: Designing Environmental Policy*, (Oxford University Press, 1998)
- Gureev, V., *Problems of Protection of Rights and Interests of Shareholders in Russian Federation* [Гуреев, В., *Проблемы защиты прав и интересов акционеров в Российской Федерации*], (WoltersKluwer, 2007)
- Hall, P. and Soskice, D., *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage*, (Oxford University Press, 2001)
- Hancher, L., *Regulating for Competition: Government, Law, and the Pharmaceutical Industry in the United Kingdom and France*, (Oxford University Press, 1990)
- Hannigan, B., 'Drawing Boundaries between Derivative Claims and Unfairly Prejudicial Petitions' (2009) *Journal of Business Law* 1
- Hansmann, H., and Kraakman, R., 'The Essential Role of Organizational Law' (2000) 110 *The Yale Law Journal* 387
- Hart, O. and Moore, J', 'Incomplete Contracts and Renegotiation' (1998) 56 *Econometrica* 755
- Hay, B., 'Allocating the Burden of Proof' (1996) 72 *Indiana Law Journal* 651
- Heise, M., 'The Past, Present, and Future of Empirical Legal Scholarship: Judicial Decision Making the New Empiricism' (2002) 2002 *University of Illinois Law Review* 819
- Hendley, K. et al, *Law Works in Russia: the Role of Law in Inter-enterprise Transactions* in Murrel, P., (ed.), *Assessing the Value of Law in Transition Economies*, (University of Michigan Press, 2001) p.p. 56-88
- Hendley, K., 'Business Litigation in the Transition: A Portrait of Debt Collection in Russia' (2004) 38 *The Law & Society Review* 305
- Hendrix, G., *The Experience of Home Litigants in Russia's Commercial Courts* in Murrel, P., (ed.), *Assessing the Value of Law in Transition Economies*, (University of Michigan Press, 2001) p.p.94- 120
- Hill, J., 'Comparative Corporate Governance and Russia – Coming Full Circle'
- Hobbes, T., *Leviathan*, (Oxford University Press, 1996)
- Hoel, T., 'Corporate Standing' (1975) *Journal of Corporation Law* 186
- Hofstede, G., *Cultures and Organizations: Intercultural Cooperation and Its Importance for Survival*, (HarperCollins Publishers, 1991)

- Hood, C. C., *The Tools of Government: Public Policy and Politics*, (Chatham House Publishers, 1983)
- Hopt, K. J., 'Shareholder Rights and Remedies: A View from Germany and the Continent' (1997) 2 *Company Financial and Insolvency Law Review* 261
- Hopt, K.J., Wymeersch, E., *Capital Markets and Company Law*, (Oxford University Press, 2003)
- Hopt, K. J., Wymeersch, E., Kanda, H., and Baum, H., *Corporate Governance in Context Corporations, States, and Markets in Europe, Japan, and the US*, (Oxford University Press, 2005)
- Horowitz, M. J., *The Transformation of American Law, 1870 – 1960*, (Oxford University Press, 1992)
- Institute of Corporate Law and Governance, *Review of Corporate Governance: OAO Rosneft Purneftegaz* (2002)
- Ioncev, M., *Joint Stock Societies* [Ионцев, М., *Акционерные общества*], (Os' 89, 2002)
- Iwasaki, I., 'The Determinants of Board Composition in a Transforming Economy: Evidence from Russia', (2008) 14 *Journal of Corporate Finance* 532
- Jagic, T., Podobnik, B., and Kolanovic, M., 'Does the Efficient Market Hypothesis Hold?' (2005) 43 *Eastern European Economics* 79
- Jarkov, V., 'Derivative Claims: Problems of Theory and Practice' (2007) 11 *Corporate Jurist* 52
- Jensen M and Meckling W, 'Theory of the firm: managerial behaviour, agency costs and ownership structure' (1976) 3 *Journal of Financial Economics* 305
- Johnson, S., et al, *Corporate governance in the Asian financial crisis* (2000) 58 *Journal of Financial Economics* 141.
- Johnson, S., McMillan, J., and Woodruff, C., 'Courts and Relational Contracts' (2002) 18 *The Journal of Law, Economics and Organization* 221
- Johnston, J., 'Bargaining Under Rules Versus Standards' (1995) 11 *Journal of Law, Economics and Organisation* 256
- Kaplow, L., 'Rules Versus Standards: An Economic Analysis' (1992) 42 *Duke Law Journal* 557
- Kaplow, L., 'The Value of Accuracy in Adjudication: An Economic Analysis' (1994) 23 *Journal of Legal Studies* 307

- Kaplow, L., 'A Model of the Optimal Complexity of Legal Rules' (1995) 11 *The Journal of Law, Economics and Organization* 151
- Kaplow, L., and Shavell, S., 'Do Liability Rules Facilitate Bargaining? A Reply to Ayres and Talley' (1995) 105 *The Yale Law Journal* 221
- Kaplow, L., and Shavell, S., 'Property Rules Versus Liability Rules: An Economic Analysis' (1996) 109 *Harvard Law Review* 715
- Kazmin, D., 2011, Codification of Relatives [Казьмин, Д., Кодификация родственников], *Vedomosti*, 23 August, available at http://www.vedomosti.ru/newspaper/article/266066/kodifikaciya_rodstvennikov. Accessed on 6 March 2014
- Kershaw, D., 'Lost in Translation: Corporate Opportunities in Comparative Perspective' (2005) 25 *The Oxford Journal of Legal Studies* 603
- Kershaw, D., *Company Law in Context: Text and Materials*, (Oxford University Press, 2009)
- Koh, P., 'Directors' Fiduciary Duties: Unthreading the Joints of Shareholder Ratification' (2005) 5 *Journal of Corporate Law Studies* 364
- Kommersant, 2001, Bonum-1 is Held Insolvent [Коммерсант, «Бонум-1» признан банкротом], *Kommersant*, 22 November, available at <http://www.kommersant.ru/news/927120>. Accessed on 6 March 2014
- Kommersant, 2003, NTV-Plus and ZAO «Bonum-1» have Agreed without the Court [Коммерсант, «НТВ-Плюс» и ЗАО «Бонум-1» договорились без суда], *Kommersant*, 16 June, available at <http://www.kommersant.ru/news/964520>. Accessed on 6 March 2014
- Krier, J., and Schwab, S., 'Property Rules and Liability Rules: The Cathedral in Another Light' (1995) 70 *New York University Law Review* 441
- Kraakman, R. et al., *The Anatomy of Corporate Law: A Comparative and Functional Approach*, (Oxford University Press, 2004)
- Kraakman, R. et al., *The Anatomy of Corporate Law: A Comparative and Functional Approach*, 2nd edn. (Oxford University Press, 2009)
- Licht A., 'The Mother of All Path Dependencies: Toward a Cross-cultural Theory of Corporate Governance Systems' (2001) 26 *Delaware Journal of Corporate Law* 147
- La Porta, R., Lopez-de-Silanes, F., Shleifer, A., Vishny, R., 'Law and finance' (1998) *Journal of Political Economy* 106

- La Porta, R., Lopez-de-Silanes, F., Shleifer, A., 'Corporate ownership around the world' (1999) *Journal of Finance* 54
- La Porta, R., Lopez-de-Silanes, F., Shleifer, A., Vishny, R., 'Investor protection and corporate governance' (2000) *Journal of Financial Economics* 58, 3–27.
- Law Commission of England & Wales, *Shareholder Remedies*, (1990)
- Lee, R., 'Fiduciary Duty Without Equity: 'Fiduciary Duties' of Directors Under the Revised Company Law of the PRC' (2006) 47 *Virginia Journal of International Law* 897
- Levine, R., 'Financial development and economic growth: views and agenda' (1997) 35 *Journal of Economic Literature* 688
- Levmore, S., 'Monitors and Free riders in Commercial and Corporate Settings' (1982) 92 *The Yale Law Journal* 49
- Levmore, S., 'Explaining Restitution', (1985) 71 *Virginia Law Review* 65
- Levmore, S., 'Variety and Uniformity in the Treatment of Good-Faith Purchaser' (1987) 16 *The Journal of Legal Studies* 43
- Levmore, S., 'Unifying Remedies: Property Rules, Liability Rules, and Starting Rules' (1996) 106 *The Yale Law Journal* 2149
- Lowry, J. and Edmunds, R., 'The Continuing Value of Relief for Directors' Breach of Duty' (2003) *Modern Law Review* 195
- Macey, J., 'Corporate Law and Corporate Governance: a Contractual erspective' (1993) 18 *Journal of Corporation Law* 185
- Machiavelli, N., *The Prince*, (Penguin Books, 1961)
- MacNeil, I., 'Company Law Rules: An Assessment From the Perspective of Incomplete Contract Theory' (2001) 1 *Journal of Corporate Law Studies* 107
- Maleshin, D., 'The Russian Style of Civil Procedure' (2007) 21 *Emory International Law Review* 543
- Marsh, H. Jr., 'Are Directors Trustees?' (1966) 22 *The Business Lawyer* 35
- McBarnet, D., and Whelan, C., *Creative Accounting and the Cross-Eyed Javelin Thrower*, (John Wiley & Sons, 1999)
- McCahery, J., et al (eds), *Corporate Governance Regimes: Convergence and Diversity*, (Oxford University Press, 2002)
- McMillan, J., and Woodruff, C., 'The Central Role of Entrepreneurs in Transition Economies' (2002) 16 *Journal of Economic Perspectives* 153

- Milhaupt, C. (ed.), *Global Markets, Domestic Institutions*, (Columbia University Press, 2003)
- Mokal, R., *Corporate Insolvency Law – Theory and Application* (Oxford University Press, 2005)
- Murrel, P., (ed.), *Assessing the Value of Law in Transition Economies*, (University of Michigan Press, 2001)
- Mogilevskii, S., *Legal Foundations of the Activities of the Joint Stock Societies* [Могилевский, С., *Правовые основы деятельности акционерных обществ*], (M. Delo, 2004)
- Nenova, T., ‘The Value of Corporate Voting Rights and Control: A Cross-Country Analysis’ (2003) 68 *Journal of Financial Economics* 325.
- North, D., *Institutions, Institutional Change and Economic Performance*, (Cambridge University Press, 1990)
- North, D., *Understanding the Process of Economic Change*, (Princeton University Press, 2005)
- Novoselov, A. and Mametov, R., ‘On Transactions in the Completion of Which There is a Conflict of Interest’ [Новоселов, А., Маметов, Р., ‘О сделках, в совершении которых имеется заинтересованность’], (2000) 12 *Vestnik Vyshego Arbitrazhnogo Suda* 83
- Ochoa, T. and Wistrich, A., ‘The Puzzling Purposes of Statutes of Limitation’ (1997) 28 *Pacific Law Journal* 454
- Oda, H., *Russian Commercial Law*, 2nd edn. (Martinus Nijhoff Publishers, 2007)
- Owen, T., *The Corporation under Russian Law, 1800 – 1917: A Study in Tsarist Economic Policy*, (Cambridge University Press, 1991)
- Parker, C., Scott, C., Lacey, N., and Braithwaite, J., *Regulating Law*, (Oxford University Press, 2004)
- Parkinson, J., *Corporate Power and Responsibility: Issues in the Theory of Company Law*, (Oxford University Press, 1993)
- Parkinson, J., Gamble, A., and Kelly, G., *The Political Economy of the Company*, (Hart Publishing, 2000)
- Payne, J., ‘A Re-Examination of Ratification’ (1999) 58 *The Cambridge Law Journal* 604
- Payne, J., ‘“Clean” hands in Derivative Actions’ (2002) 61 *The Cambridge Law Journal* 76
- Pease, D., ‘Aronson V. Lewis: When Demand is Excused and Delaware’s Business Judgment Rule’ (1984) 9 *Delaware Journal of Corporate Law* 39

- Pettet, B., *Company Law*, (Pearson Education, 2001)
- Pennington, R., *Company Law*, 8th edn. (Butterworths, 2001)
- Peritz, R., *Competition Policy in America: History, Rhetoric, Law*, (Oxford University Press, 1996)
- Picciotto, S., *International Business Taxation*, (Quorum Books, 1992)
- Pistor, K., 'Supply and Demand for Contract Enforcement in Russia: Courts, Arbitration, and Private Enforcement' (1996) 22 *Review of Central and East European Law* 55
- Pistor, K., 'Legal Ground Rules in Coordinated and Liberal Market Economies' (2005) ECGI Working Paper No. 30
- Pistor, K., Raiser, M., Gelfer, S., *Law and finance in transition economies* (2000) *Economics of Transition* 8
- Pistor, K., and Xu, C., 'Fiduciary Duty in Transitional Civil Law' (2002) ECGI, Working Paper No. 1
- Pistor, K., and Xu, C., 'Fiduciary Duty in Transitional Civil Law Jurisdiction: Lessons from the Incomplete Law Theory' in Milhaupt, C., *Global Markets, Domestic Institutions*, (Columbia University Press, 2003)
- Pistor, K., and Xu, C., *Governing Emerging Stock Markets: Legal vs Administrative Governance* (2005) 13(1) *Corporate Governance* 5
- Png, 'Optimal Subsidies and Damages in the Presence of Judicial Error (1986) 6 *International Review of Law and Economics* 101
- Polinsky, A. M., and Shavell, S., 'Legal Error, Litigation and the Incentive to Obey to the Law' (1989) 5 *Journal of Law, Economics, and Organization* 99
- Posner, R. A., 'An Economic Approach to the Law of Evidence' (1998) 51 *Stanford Law Review* 1477
- Posner, R. A., *Economic Analysis of Law*, 5th edn. (Aspen Law & Business, 1998a)
- Posner, R. A., *Frontiers of Legal Theory*, (Harvard University Press, 2001)
- Posner, R. A., *How Judges Think*, (Harvard University Press, 2008)
- Power, M., *The Audit Society: Rituals of Verification*, (Oxford University Press, 1997)
- Prentice, D., 'The Theory of the Firm: Minority shareholder Oppression: sections 459-461 of the Companies Act 1985' (1988) 8 *Oxford Journal of Legal Studies* 55

- Ryanykh, G., 2001a, The Court Permitted «Media-Most» not to Repay Debts [Пьяных, Г., Суд разрешил 'Медиа-Мосту' не возвращать долги], *Kommersant*, 16 February, available at <http://www.kommersant.ru/doc/168655?isSearch=True>. Accessed on 6 March 2014
- Ryanykh, G., 2001b, The Last Broadcast is Coming [Пьяных, Г., Последний показ наступает], *Kommersant Vlast*, 10 April, available at <http://www.kommersant.ru/doc/253430?isSearch=True>. Accessed on 6 March 2014
- Radygin, A., and Entov, R., 'Enforcement of Property Rights and Contractual Obligations' (2003) 46 *Problems of Economic Transition* 7
- Raiffa, H., *Decision Analysis: Introductory Lectures on Choices under Uncertainty*, (Addison-Wesley Publishing, 1968)
- Rajak, H., *Sourcebook of Company Law*, 2nd edn. (Jordan Publishing, 1995)
- Reese, W., and Weisbach, M., 'Protection of minority shareholder interests, cross-listings in the United States, and subsequent equity offerings' (2002) 66 *Journal of Financial Economics* 65
- Reisberg, A., *Derivative Actions and Corporate Governance: Theory and Opinion*, (Oxford University Press, 2007)
- Reshetnikova, I. V., 'The Role of Courts in Adversarial Litigation in Russia (2009) 34 *Review of Central and East European Law* 1
- Roe, M. J., *Strong Managers, Weak Owners: The Political Roots of American Corporate Finance*, (Princeton University Press, 1994)
- Roe, M. J., *Political Determinants of Corporate Governance: Political Context, Corporate Impact* (Oxford University Press, 2003)
- Rozhkova, M., 'Again on Class and Derivative Actions' [Рожкова, М., 'И вновь о групповых и косвенных исках'], (2007) 5 *Vestnik Vyshego Arbitrazhnogo Suda* 19
- Romano R., Answering the wrong question: the tenuous case for mandatory corporate laws (1989) 89 *Columbia Law Review* 1599.
- Romano, R., 'The Shareholder Suit: Litigation Without Foundation?' (1991) 7 *The Journal of Law, Economics and Organization* 55
- Rose, C. M., 'The Shadow of The Cathedral' (1996) 106 *The Yale Law Journal* 2175
- Rosenberg, D., and Shavell, S., 'A Model in which Suits are Brought For Their Nuisance Value' (1985) 5 *International Review of Law and Economics* 3
- Rubin, G. R., and Sugarman, D., *Law Economy & Society*, (Professional Books, 1984)

- Sachs, J. D., and Pistor, K., *The Rule of Law and Economic Reform in Russia*, (Westview Press, 1997)
- Schmitz, P. W., 'The Hold-Up Problem and Incomplete Contracts: A Survey of Recent Topics in Contract Theory' (2001) 53 *Bulletin of Economic Research* 1
- Schwartz, A., 'Relational Contracts in the Courts: An Analysis of Incomplete Agreements and Judicial Strategies' (1992) 21 *The Journal of Legal Studies* 271
- Schwartz, A., and Scott, R. E., 'Contract Theory and the Limits of Contract Law' (2003) 113 *The Yale Law Journal* 541
- Schwartz, D. E., 'In Praise of Derivative Suits: A Commentary on the Paper of Professors Fischel and Bradley' (1985) 71 *Cornell Law Review* 322
- Scott, W. R., *Financial Accounting Theory*, 3rd edn. (Prentice Hall, 2003)
- Schuster, E., 'Efficiency in Private Control Sales – The Case for Mandatory Bids' (2010) LSE Law, Society and Economy Working Papers 08/2010
- Sepe, S., 'Private Sale of Corporate Control: Why the European Mandatory Bid Rule is Inefficient' (2010) *Arizona Legal Studies Discussion Paper No. 10-29 SSRN*
- Shapkina, G., *The New in the Russian Shareholder Legislation: Amendments and Additions to the Joint Stock Companies Act* [Шапкина, Г., *Новое в российском акционерном законодательстве (изменения и дополнения Федерального закона "Об акционерных обществах")*], (Bulletin Vysshego Arbitrazhnogo Suda, 2002)
- Shapkina, G., *Application of Corporate Legislation* [Шапкина Г., *Применение акционерного законодательства*], (Statut, 2009)
- Shavell, S., 'Individual Precautions To Prevent Theft: Private Versus Socially Optimal Behaviour' (1991) 11 *International Review of Law and Economics* 123
- Shavell, S., *Foundation of Economic Analysis of Law*, (Harvard, 2004)
- Shestakova, N., 'Transactions Under the Russian Civil Code: Invalidity and the Protection of Rights' (1998) 24 *Review of Central and East European Law* 429
- Shestakova, N., *Invalidity of Transactions* [Шестакова, Н., *Недействительность сделок*] (Yuridichesky Center Press, 2008)
- Shitkina, I., 'The Legal Position of the Board of Directors in the Light of the Amendments to Federal Act on the Joint Stock Companies' [Шиткина, И., 'Правовое положение совета директоров в свете изменения Федерального закона Об акционерных обществах'] (2002) 1 *Economics and Law* 73

- Shitkina, I., *Corporate Law* [Шиткина, И., *Корпоративное право*], (WoltersKluwer, 2008)
- Shitkina, I., *Holdings. Regulation and Corporate Governance* [Шиткина, И., *Холдинги: правовое регулирование и корпоративное управление*], (WoltersKluwer, 2008a)
- Siems, M., *Convergence in Shareholder Law: International Corporate Law and Financial Market Regulation*, (Cambridge University Press, 2008)
- Simachev, I., 'The Institution of Bankruptcy in Russia' (2003) 46 *Problems of Economic Transition* 32
- Sprenger, C., 'Ownership and Corporate Governance in Russian Industry: A Survey' (2002) European Bank for Reconstruction and Development, Working Paper no. 70
- Sypnowich, C., *The Concept of Socialist Law*, (Oxford University Press, 1990)
- Tamanaha, B., *A General Jurisprudence of Law and Society*, (Oxford University Press, 2001)
- Tamahana, B., 'The Primacy of Society and the Failure of Law and Development' (2009) Legal Studies Research Paper Series, Paper No. 9-0172
- Tavernise, S., 2000, Using Bankruptcy as a Takeover Tool; Russian Law Puts Healthy Companies at Risk, *The New York Times*, 7 October
- Telukina, M., *Commentary on the Federal Law on Joint Stock Companies* [Телюкина, М., *Комментарий к Федеральному закону Об акционерных обществах*], (Wolters Kluwer, 2005)
- Teubner, G., 'How the Law Thinks: Toward a Constructivist Epistemology of Law' (1989) 23 *Law & Society Review* 727
- Thompson, R., 'The Public and Private Faces of Derivative Law Suits' (2004) 57 *Vanderbilt Law Review* 1747
- Travis Laster, J., 'Goodbye to the Contemporaneous Ownership Requirement' (2008) 33 *Delaware Journal of Corporate Law* 673
- Treushnikov, M., *Arbitrazh Procedure* [Треушников, М., *Арбитражный процесс*], (JSC Publishing House Gorodec, 2005)
- Trubeck D. and Galanter M., 'Scholars in Self-estrangement: Some Reflections on Crisis in Law and Development Studies in the United States' (1974) *Wisconsin Law Review* 1062
- Trubek, D., and Santos, A., *The New Law and Economic Development: A Critical Appraisal*, (Cambridge University Press, 2006)
- Vereshchagin, A., *Judicial Law-Making in Post-Soviet Russia*, (Routledge-Cavendish, 2007)

- Vitrianskii, V., 'Contrast as a Means for Regulating Market Relations: The Draft Civil Code (First Part) of the Russian Federation' (1994) 20 *Review of Central and East European Law* 649
- Volkov, V., 'Hostile Enterprise Takeovers: Russia's Economy in 1998 – 2002' (2004) 29 *Review of Central and East European Law* 527
- Williamson, O., 'Credible Commitments: Using Hostages to Support Exchange' (1983) 73 *The American Economic Review* 519
- Williamson, O., *The Economic Institutions of Capitalism*, (The Free Press, A division of Macmillan, 1985)
- Whincop, M., *An Economic and Jurisprudential Genealogy of Corporate Law*, (Dartmouth Publishing Company, Ashgate Publishing, 2001)
- Whincop, M., 'Contracting Around the Conflict Rule: An Empirical Analysis of a Penalty Default' (2002) 2 *Journal of Corporate Law Studies* 1
- Whincop, M., and Armour, J., 'The Proprietary Foundations of Corporate Law' (2007) 27 *Oxford Journal of Legal Studies* 429
- Worthington, S., *Equity*, (Oxford University Press, 2003)
- Worthington, S. and Sealy, L., *Cases and Materials in Company Law*, 8th edn. (Oxford University Press, 2008)
- Yablon, C., 'On the Allocation of Burdens of Proof in Corporate Law: An Essay on Fairness and Fuzzy Sets' (1991) 13 *Cardozo Law Review* 497
- Yakovlev, A., 'Evolution of Corporate Governance in Russia: Government Policy vs. Real Incentives of Economic Agents' (2004) 16 *Post-Communist Economies* 387
- Yeager, P. C., *The Limits of Law: The Public Regulation of Private Pollution*, (Cambridge University Press, 1991)